SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No.

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, ET AL., PETITIONERS,

vs.

JOHN GERDES AND JAMES D. CARPENTER, JR., TRUSTEES OF REYNOLDS INVESTING CO., INC., DEBTOR

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

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[fol. 1]

IN THE SUPREME COURT OF NEW YORK, APPELLATE DIVISION, FIRST DEPARTMENT

In the Matter of the Application of

B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler and Murray MacElhinny, individually and as co-partners doing business up to the close of business October 31, 1941 under the firm name and style of Kellogg, Emery & Inness-Brown and

Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst Petitioners-Respondents,

for an order fixing the amount to which petitioners are entitled as compensation and for the determination and enforcement of their liens for services rendered in a certain action in this court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti et al., Defendants; and a certain action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward, Defendants, and a certain action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendants.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondent-Appellants

Statement Under Rule 234

[fol. 2] Appellants appeal from an order dated March 26, 1942 overruling appellants' objections to the jurisdiction of the Court; an order dated April 15, 1942 fixing the amount

to which respondents are entitled as compensation and determining respondents have a lien for services rendered; and from an order dated April 29, 1942 denying appellants' motion to resettle order dated April 15, 1942.

This proceeding was commenced by service of notice and petition on December 23, 1941.

The answer of respondents was served January 12, 1942.

The reply was served January 16, 1942.

The original petitioners are the law firms of Kellogg, Emery & Inness-Brown and Greenbaum, Wolff & Ernst.

The respondents are John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor.

Petitioner's attorneys are Satterlee & Warfield and Greenbaum, Wolff & Ernst.

Respondents are appearing pro se.

There has been no change of parties or attorneys herein.

A notice of appeal from the order dated March 26, 1942 was served on April 23, 1942 and filed on April 24, 1942. The notice of appeal from an order dated April 15, 1942 which also provides for the review of the order dated March 26, 1942 and the order dated April 29, 1942 was served and filed on May 7, 1942.

[fol. 3] In Supreme Court of New York, New York County

[Title omitted]

Notice of Appeal from Order Overruling Respondents' Objections to Jurisdiction of the Court—April 23, 1942

[fol. 4] Sirs:

Please Take Notice that John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, the respondents in the above special proceeding hereby appeal to the Appellate Division of the Supreme Court, First Department, from the order dated March 26, 1942, in said proceedings and entered in the office of the Clerk of the County of New York on March 27, 1942, overruling respondents' objections to the jurisdiction of the

Court, and this appeal is taken from the whole and from each and every part of said order.

Dated, April 23, 1942.

Yours, etc., John Gerdes and James D. Carpenter, Jr., As Trustees of Reynolds Investing Company, Inc., Debtor, Respondents, Pro Se, One Wall Street, Borough of Manhattan, New York City.

To: Satterlee & Warfield, 49 Wall Street, New York, New York; Greenbaum, Wolff & Ernst, 285 Madison Avenue, New York, New York, Attorneys for Petitioners. Archibald R. Watson, Esq., Clerk of the County of New York.

[fol. 5] In Supreme Court of New York, New York County

Notice of Appeal From Order Overruling Respondents' Objections to Jurisdiction of the Court, Order Fixing Lien and Amount of Attorneys' Compensation and Order Denying Motion to Resettle Said Order—May 6, 1942

[Title omitted]

[fol. 6] Sirs:

Please Take Notice that John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, respondents, hereby appeal to the Appellate Division of the Supreme Court, First Department, from the order dated and entered in the above entitled proceeding in the office of the Clerk of the County of New York on the 15th day of April, 1942 adjudging that the petitioners have a lien to the extent of $102,250. upon the judgment entered in a certain cause of action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti, et al., Defendants; and adjudging that the petitioners have a lien to the extent of $2,045. upon a cause of action in an action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward, Defendants; and adjudging that the peti-

tioners have a lien to the extent of $766.87 upon a cause of action in an action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendant and from each and every part thereof.

Please Take Notice that said John Gerdes and James D. [fol. 7] Carpenter, Jr., as Trustees of Reynolds Investing Co., Inc., Debtor, respondents, appeal from and will bring up for review an order made in the above entitled proceeding, dated March 26, 1942, and entered in the office of the Clerk of the County of New York on March 27, 1942, overruling respondents' objections to the jurisdiction of the Court and from the whole and from each and every part of said order.

Please Also Take Notice that said John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Co., Inc., Debtor, respondents, appeal from and will bring up for review an order made in the above entitled proceeding, dated April 29, 1942, and filed in the office of the Clerk of the County of New York on April 30, 1942, denying respondents' motion for resettlement of the order of April 15, 1942 hereinbefore referred to, and from the whole and from each any every part of said order.

Dated May 6, 1942.

Yours, etc., John Gerdes and James D. Carpenter, Jr., As Trustees for Reynolds Investing Company, Inc., Debtor, Respondents, Pro Se, Office and Post Office Address, One Wall Street, Borough of Manhattan, New York City.

[fol. 8] To: Satterlee & Warfield, Esqs., 49 Wall Street, New York City; Greenbaum, Wolff & Ernst, Esqs., 285 Madison Avenue, New York City, Attorneys for Petitioners. Archibald R. Watson, Esq., Clerk of the County of New York.

In Supreme Court of New York, New York County

Order Overruling Respondents' Objections to Jurisdiction of the Court Appealed From—Filed March 27, 1942

At a Special Term, Part I, of the Supreme Court of the State of New York, held in and for the County of New

York, at the Court House, Foley Square, on the 26th day of March, 1942.

Present—Hon. Carroll G. Walter, Justice.

The petitioners having moved this Court for an order fixing the amount to which they are entitled as compensation and for the determination and enforcement of their liens for services rendered in the above-entitled actions, and respondents having filed an answer questioning the jurisdiction of this Court, and said motion having duly come [fol. 9] on to be heard before me, and the Court having by its opinion appearing in the New York Law Journal March 6, 1942 overruled respondents' objections to the jurisdiction of the Court and granted respondents ten days from publication of said opinion to answer further with respect to the merits, and having thereafter further extended respondents' time to so answer to March 20, 1942, and respondents having elected not an answer further on the merits,

Now, on reading and filing the notice of motion and petition herein, both dated December 22, 1941, and the affidavit of David Paine, sworn to January 15, 1942, in support of said motion and the answer of respondents verified January 12, 1942, in opposition thereto, and after hearing David Paine, of Counsel for petitioners, in support of the motion, and John Gerdes pro se of Counsel in opposition thereto, and due deliberation having been had, and upon the filing of the opinion of the Court,

It is, on motion of Satterlee & Warfield and Greenbaum, Wolff & Ernst, attorneys for petitioners,

Ordered that the objections to the jurisdiction of the Court, as set forth in the answer of respondents, are hereby overruled to which ruling respondents duly excepted; and it is further

Ordered that the matter be and hereby is set down for hearing upon the merits before me in the Bronx County Court House, Trial Term Part III, at 2 o'clock P. M. on [fol. 10] March 31, 1942, to assess the value of services rendered by petitioners in the above-entitled actions, and to determine and enforce their liens thereto for such services.

Enter, C. G. W., Justice of the Supreme Court.

Filed March 27, 1942.—New York County Clerk's Office.

IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

ORDER FIXING LIEN AND AMOUNT OF ATTORNEYS' COMPENSATION APPEALED FROM—April 15, 1942

Present:— Hon. Carroll G. Walter, *Justice*.

The issues in this proceeding having come on duly for hearing on the 31st day of March, 1942, pursuant to the intermediate order herein of March 26, 1942, and John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Respondents, at that time having advised the Court by John Gerdes, Esq. that they [fol. 11] were appearing specially herein to request the Court to adjourn said hearing until the determination by the Appellate Division of an application therein by respondents for an order under Article 78 of the Civil Practice Act prohibiting the Court from proceeding herein, and said respondents having stated then and there that the Appellate Division had denied an application by said respondents for a stay of the proceedings herein, and said request for an adjournment having been denied, and the respondents having been directed by the Court to proceed herein, and said respondents having declined to proceed, and proof having been taken of the services rendered by petitioners, and at the conclusion thereof the Court having adjourned said hearing until April 8, 1942 for the express purpose of giving respondents an opportunity of presenting any matter relevant to the issues herein and particularly to advise the Court with respect to their opinion of the value of the services rendered by petitioners, and respondents having been duly advised of said adjournment and the purposes thereof, and having defaulted in appearing at the adjourned hearing on April 8, 1942, and the Court having thereupon duly fixed the fair and reasonable value of the services rendered by petitioners as attorneys for respondents in the action herein first above entitled at the sum of $100,000, and in the action herein second above entitled at the sum of $2,000, and in the action herein third above entitled at the sum of $750,

Now, it is, upon motion of Satterlee & Warfield and Greenbaum, Wolff & Ernst, attorneys for petitioners, [fol. 12]—Ordered, adjudged and decreed that the petitioners B. H. Inness Brown, David Paine, Ethelbert War-

field, J. Fearon Brown, George Koegler and Murray MacElhinny, individually and as co-partners, doing business up to the close of business October 31, 1941 under the firm name and style of Kellogg, Emery & Inness-Brown, of 49 Wall Street, Borough of Manhattan, City of New York, and Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, of 285 Madison Avenue, Borough of Manhattan, City of New York, be, and they hereby are, adjudged to have a lien to the extent of $100,000 with interest from November 27, 1941 amounting to $2,250, amounting in all to $102,250 upon the judgments entered in a certain action in this Court (described in the petition herein as Action No. 1) entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti, et al., Defendants, and the proceeds thereof in whatever hands they may come, including, without limiting the foregoing, any sum of money or other consideration paid or to be paid by any defendant in said action in settlement of said judgments, and that petitioners may enforce said liens in any mannner permitted by law; and it is further

Ordered, adjudged and decreed that the petitioners B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler and Murray MacElhinny, indi- [fol. 13] vidually and as co-partners, doing business up to the close of business October 31, 1941 under the firm name and style of Kellogg, Emery & Inness-Brown, of 49 Wall Street, Borough of Manhattan, City of New York, and Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, of 285 Madison Avenue, Borough of Manhattan, City of New York, be, and they hereby are, adjudged to have a lien to the extent of $2,000 with interest from November 27, 1941 amounting to $45.00 amounting in all to $2,045.00 upon plaintiffs' cause of action in an action in this Court (described in the petition herein as Action No. 2) entitled John Gerdes and James

D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward, Defendants, and that said lien attaches to any verdict, report, determination, decision, judgment or final order in plaintiffs' favor therein and the proceeds thereof in whatever hands they come, including, without limiting the foregoing, any sum of money or other consideration paid or to be paid by any defendant in said action in settlement of said judgments and that petitioners may enforce said lien in any manner permitted by law; and it is further

Ordered, adjudged and decreed that the petitioners B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler and Murray MacElhinny, individually and as co-partners, doing business up to the close of business October 31, 1941 under the firm name and style [fol. 14] of Kellogg, Emery & Inness-Brown, of 49 Wall Street, Borough of Manhattan, City of New York, and Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, of 285 Madison Avenue, Borough of Manhattan, City of New York, be, and they hereby are, adjudged to have a lien to the extent of $750 with interest from November 27, 1941 amounting to $16.87, amounting in all to $766.87 upon plaintiffs' cause of action in an action in this Court (described in the petition herein as the Globe Action) entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendant, and that said lien attaches to any verdict, report, determination, decision, judgment or final order in plaintiffs' favor therein and the proceeds thereof in whatever hands they come, including without limiting the foregoing any sum of money or other consideration paid or to be paid by the defendant in said action in settlement of said judgments and that petitioners may enforce the same in any manner permitted by law; and it is further

Ordered, adjudged and decreed that petitioners may apply at the foot hereof for additional and further relief to enforce said liens.

Enter: C. G. W. Justice of the Supreme Court of the State of New York.

[fol.15] In Supreme Court of New York, New York County
Order Denying Motion to Resettle Order, Dated April 15, 1942, Appealed from—Filed April 30, 1942

Present—Hon. Carroll G. Walter, *Justice*.

The following papers numbered 1 to 5 read on this motion submitted and referred this 27 day of April, 1942.
Calendar No. 119.

	Papers Numbered
Notice of Motion and Affidavits Annexed	1 to 3
Answering Affidavits	4
Filed Papers (County Clerk's Office)	
Order of April 15	5

Upon the foregoing papers this motion to resettle final order of April 15, 1942 is denied. It is a strange notion that a litigant may deliberately refrain from attending a hearing before a court and yet convey allegedly pertinent ideas and information by means of a letter to the judge. The court will tolerate no such practice. As the United States delivers mail to whomsoever it is addressed, the judge is powerless to protect himself against physical receipt of such a letter, [fol. 16] but for judicial purposes the court treats the letter as non-existent.

Dated: April 29, 1942.
C. G. W., *J. S. C.*
Filed April 30, 1942.
New York County Clerk's Office.

In Supreme Court of New York, New York County

Notice of Motion.—December 22, 1941

Sirs:

Please take notice that upon the annexed petition duly verified December 22, 1941, the undersigned will move this Court at a Special Term, Part I thereof, to be held at the County Court House, Worth and Centre Streets, New York City, on the 12th day of January, 1942, at 10:00 A. M. in the forenoon thereof, or as soon thereafter as counsel can be heard, for an order fixing the amount to which petitioners are entitled as compensation and for the determination and

enforcement of their liens for services rendered in the above-entitled actions.

Dated: December 22, 1941.

Satterlee & Warfield, 49 Wall Street, New York City.
[fol. 17] Greenbaum, Wolff & Ernst, 285 Madison Avenue, New York City, Attorneys for Petitioners.

To: John Gerdes, Esq., 1 Wall Street, New York City, New York, and James D. Carpenter, Esq., 75 Montgomery Street, Jersey City, New Jersey, Trustees of Reynolds Investing Company, Inc., Debtor.

[fol.18] IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

PETITION OF B. H. INNESS BROWN, ET AL.—December 22, 1941

[Title omitted]

To the Supreme Court, New York County:

The petition of B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler and Murray MacElhinny, individually and as co-partners doing business up to the close of business October 31, 1941 under the firm name and style of Kellogg, Emery & Inness Brown, which firm was dissolved on said date, and Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of [fol. 19] Greenbaum, Wolff & Ernst, respectfully shows to this Court and alleges:

I. The firms of Kellogg, Emery & Inness Brown and Greenbaum, Wolff & Ernst, are attorneys of record for the plaintiffs in a certain action pending in this Court wherein the plaintiffs are John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, and Clarence K. Reynolds, et al. are defendants (hereinafter called Action No. 1.); said firms are attorneys of record for plaintiffs in an action pending in this Court wherein the plaintiffs are John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, and Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward are defendants (hereinafter

called Action No. 2); and said firms are attorneys of record for plaintiffs in an action in this Court wherein John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, are plaintiffs, and wherein the defendant is Globe Indemnity Co. (hereinafter called the Globe Action).

II. On or about May 18, 1938 a petition for reorganization under the Federal Bankruptcy Act was filed against Reynolds Investing Co., Inc., a Delaware corporation (hereinafter called Investing), in the United States District Court for the District of New Jersey. As appears from said petition filed therein, the act of bankruptcy and insolvency of Investing arose from the wrongful extraction of upwards of $882,500 from the treasury of Investing in or about December, 1937 and January, 1938.

[fol. 20] III. On June 21, 1938 three of the four members of the Board of Directors of Investing resigned and, pursuant to an arrangement approved by Judge Fake of said United States District Court, they elected as their successors Arthur T. Vanderbilt, then the President of the American Bar Association, Fred G. Stickel, Jr., former Common Pleas Judge of the State of New Jersey, and Charles F. Lynch, former United States District Judge for the District of New Jersey.

On June 22, 1938 said Board of Directors of Investing passed a resolution instructing the New Jersey counsel for Investing to consult with your petitioners' firms to determine what, if any, action should be taken against certain former officers and directors of Investing and others to recover moneys improperly taken from Investing's treasury and to consider other claims which Investing might have. On June 27, 1938 the said Board of Directors passed a resolution instructing your petitioners' firms to prepare a formal report on a proposed bill in equity against said former officers and directors of Investing. Pursuant thereto and on or about July 6, 1938, your petitioners' firms prepared and delivered to said Board a written report setting forth their opinion as to the liability of said former officers and directors to Investing by reason of their transfer of control and management of Investing on December 31, 1937 and the wrongful removal and sale of Investing's securities on or about December 31, 1937

and January, 1938 and the suggested procedure for enforcing said liability.

IV. On August 1, 1938, in a conference with said Board of Directors, your petitioners' firms advised said Board [fol. 21] of Directors that an action should be instituted in the Supreme Court, New York, on behalf of Investing, against said former officers and directors and certain other persons based upon their transfer of control and management of Investing on December 31, 1937 and the theft of the $882,500 in January, 1938 and other breaches of trust committed prior thereto. Acting upon said advice, said Board of Directors authorized the President of Investing to apply to Judge Fake for permission to institute an equity suit in New York to enforce the liabilities mentioned above. On August 1, 1938, Judge Fake made an order authorizing the institution of such suit or suits and the retention of your petitioners' firms to act as attorneys therein for Investing.

V. On August 4, 1938, your petitioner's firms, pursuant to the order of Judge Fake dated August 1, 1938, served upon certain of the defendants copies of the summons and complaint in Action No. 1. The causes of action in said complaint revolved about the transactions which occurred on December 31, 1937 and certain transactions which occurred in the period 1928-1932.

VI. On January 19, 1939, after a number of hearings were held in the reorganization proceedings, Judge Fake entered an order approving the petition and amended petition for reorganization and appointing John Gerdes and James D. Carpenter, Jr., Trustees of Investing. Said order of appointment provided, inter alia, that the Trustees were authorized and empowered to prosecute, become a party to or defend actions in which the debtor had an interest as plaintiffs or defendants and to be sub- [fol. 22] stituted as parties therein in the action which had been commenced pursuant to the order of the Court dated August 1, 1938, and to proceed with said action in accordance with the terms of said order. On February 10, 1939, an order was signed by Mr. Justice Shientag substituting said John Gerdes and James D. Carpenter, Jr. as Trustees of Reynolds Investing Co., Inc., Debtor, as plaintiffs in said Action No. 1.

VII. Certain motions to strike various allegations and paragraphs of the complaint and to dismiss certain causes of action contained therein were made by defendants Clarence K. Reynolds and William F. Woodward which resulted in a decision generally favorable on all points to plaintiffs. An appeal was taken by said defendants to the Appellate Division from the order of Special Term denying said motions. On February 17, 1938, the Appellate Division unanimously affirmed the order of Special Term which denied the said motions to strike out certain portions of the complaint and to dismiss certain causes of action therein. Thereafter leave to appeal from part of said order of the Appellate Division was granted and an appeal was taken to the Court of Appeals. The Court of Appeals sustained the claim of plaintiffs in so far as the action related to wrongs committed on and subsequent to December 31, 1937, but held that the cause of action in the complaint relating to wrongs committed by said directors in 1928-1932 was insufficient because it did not contain specific allegations of wrongdoing. As will appear more fully hereafter, your petitioners' firms, after consulting with and obtaining the approval of the plaintiffs, began the ac-[fol. 23] tion heretofore referred to as Action No. 2, in which there were alleged specifically the wrongdoings committed by said directors in the period 1928-1932.

VIII. A motion made by defendant Alexander H. McLanahan to dismiss the causes of action in No. 1 referring to the December 31, 1937 transaction was denied by Mr. Justice Rosenman.

IX. After issue was joined by the service of answers of twenty-five defendants in Action No 1, an order was obtained directing their examination before trial and pursuant thereto your petitioners' firm examined seventeen defendants whose testimony covered 2,000 pages. At the same time your petitioners' firms aided and cooperated with one of the Trustees, James D. Carpenter, Jr., in the examination of witnesses in New Jersey and Virginia in proceedings under 21-A of the Federal Bankruptcy Act relating to and for the purpose of preparing the New York actions, No. 1 and No. 2. In aid of said examinations before trial and generally for the preparation of the trial of Action No. 1, your petitioners' firms attended or read the minutes of the investigations of the Attorney General

of the State of New York and the Securities and Exchange Commission into the looting of certain investment trusts including Investing, attended the trial in the United States District Court of the Southern District of New York in *United States of America* v. *Paine*, and the trial at General Sessions of *People* v. *Vincent E. Ferretti, et al.*, all of which investigations and trials were of extensive nature [fol. 24] and covered many thousands of pages of testimony. Although these investigations and trials were concerned partly with the looting of other corporations, an examination thereof was necessary in order to establish the systematic plan and design of the defendants to acquire and loot Investing; that is, the looting of Investing was part of a larger conspiracy to acquire and loot investment trusts by substantially the same group of people adopting substantially similar methods.

In addition to the investigation of the many complex questions of fact, including difficult problems of valuation of securities in the portfolio of Investing, the preparation entailed research and examination covering a wide variety of questions of law, many of which were novel.

X. After a thorough and painstaking investigation of the facts and law and the examination of all appropriate parties, your petitioners' firms conducted the trial of Action No. 1 before Mr. Justice Walter at Special Term, Part III of this Court. The trial consumed six weeks, in the course of which upwards of 4,800 pages of testimony were taken and 448 exhibits introduced in evidence. At the conclusion of the trial the Court rendered a decision covering 80 pages in which he sustained the plaintiffs' action against all the important defendants and a final judgment was entered against defendants Clarence K. Reynolds and William F. Woodward in favor of plaintiffs in the sum of $73,471.61 and against the firm of Prentice & Brady in the sum of $40,886.18. The judgment further directed that the defendants Clarence K. Reynolds, William F. [fol. 25] Woodward, Vincent E. Ferretti, William D. Boehm, Franklin E. Mayer, George K. Hyslop, Sartell Prentice, Jerome C. Brady, George Clayton and Calmur & Co. account to plaintiffs for all money and property of Investing wrongfully diverted to and all profits made by them and all damages sustained by Investing and referred the matter to Philip J. Dunn, Esq. to ascertain said profits

and damages. On April 28, 1941, your petitioners' firms collected $18,659.52 on account of the liability of the firm of Prentice & Brady and delivered the same to plaintiffs. As a result of your petitioners' firms' efforts, an agreement was reached with liquidator of the firm of Prentice & Brady which makes it quite likely that within a relatively short period plaintiffs will collect an additional sum of approximately $12,500. Your petitioners' firms have also collected the sum of $2,500 from the defendant Franklin E. Mayer in full payment of said defendant's liability, which was set forth in the fifth cause of action in Action No. 1, and have delivered the same to plaintiffs.

XI. Pursuant to the aforesaid judgment, your petitioners' firms conducted hearings before Referee Dunn to fix the accountability and liability of the defendants referred to above. In connection with the reference, further investigation of fact and law was made and a number of memoranda were submitted to the Referee. On the 20th day of September, 1941, the Referee filed his report, and on the 15th day of October, 1941, said report of the Referee was confirmed by order of Mr. Justice Walter; and on the 5th day of November, 1941, judgment was entered in [fol. 26] favor of plaintiffs and against defendants as follows:

1. Clarence K. Reynolds and William F. Woodward, jointly and severally	$1,106,713.92
2. William F. Woodward individually	1,225.00
3. Jerome C. Brady, George H. Clayton, Vincent E. Ferretti and Calmur & Co., jointly and severally	1,310,109.13
4. William D. Boehm	11,538.98
5. George K. Hyslop	3,914.82
6. Franklin E. Mayer	1,088,670.23

XII. Due to the inability of plaintiffs to obtain jurisdiction of defendants R. S. Reynolds and R. S. Reynolds, Jr. who resided in Virginia, plaintiffs commenced an action against said defendants and others in the United States District Court, Eastern District of Virginia, based in part upon the identical transaction involved in Action No. 1.

Your petitioners' firms assisted in the drafting of the Virginia complaint had made the issues parallel with those raised in the New York Action to the end that the proof in New York Action No. 1 would also sustain the Virginia action. A stipulation was entered into between plaintiffs' Virginia attorneys and the attorneys for defendants therein permitting any of the parties to introduce as evidence in said action proof adduced in Action No. 1 in New York. In effect the whole case prepared by petitioners' firms was made and is available to Virginia counsel for [fol. 27] the plaintiffs and said proof should constitute the case of plaintiffs in Virginia. No compensation is sought in this application for the services performed exclusively in connection with the Virginia litigation. Reference thereto is made in this petition because of its relevance to the value of the services rendered in New York Action No. 1.

XIII. In connection with the institution of Action No. 1 and the conduct thereof your petitioners' firms spent 8,814½ hours, of which 1,778¾ hours were spent by partners and 7,035¾ hours by associates. This compilation does not include time spent by petitioner Lawrence S. Greenbaum at the trial of this action before Justice Walter, and petitioners' firms do not seek compensation for such time.

XIV. As heretofore pointed out, Action No. 2 is concerned with certain breaches of trust and acts of negligence committed by Investing's directors in the period 1928-1932. Originally incorporated as a fourth cause of action in Action No. 1, these acts and omissions were, after the decision of the Court of Appeals already referred to, set forth in a new action begun May 29, 1940 on behalf of John Gerdes and James D. Carpenter, Jr. as Trustees of Reynolds Investing Co., Inc., Debtor. Process was served upon defendants Clarence K. Reynolds and William F. Woodward, but plaintiffs were unable to serve process upon defendant Richard S. Reynolds who remained outside of the jurisdiction.

XV. Thereafter defendants Clarence K. Reynolds and [fol. 28] William F. Woodward made certain motions to strike large portions of the complaint, and these motions were in all substantial respects denied by Mr. Justice Bern-

stein, whose order thereon was thereafter affirmed unanimously by the Appellate Division, First Department.

XVI. The acts complained of in Action No. 2 are as follows:

1. Sale of United States Foil Stock.

The Board of Directors of Investing was composed of the defendants and John W. Hanes, all of whom were at the same time officers of Investing. John W. Hanes resigned as an officer in April, 1930 and as a director in September, 1931. In 1928 Investing had in its portfolio a block of United States Foil Class B Common Stock. This stock had been previously split up four-for-one, and the new shares were traded in on the New York Stock Exchange. On October 30, 1928, defendants caused Investing to sell privately 4,000 shares of said stock for $12.50 per share and other valuable property. The $12.50 per share was received by Investing, but the other property was divided among the defendants. On the day of the sale the market value of said stock on the New York Stock Exchange was $44 to $44⅜ per share. The result of this private sale was that Investing was caused to lose more than $125,000. It is alleged that the sale was not made for any legitimate corporate purpose, but for the personal interest and pecuniary benefit of the defendants to enrich themselves at Investing's [fol. 29] expense. It is further alleged that the sale was secret, made without the knowledge of the co-director and officer Hanes, and concealed from the security holders of Investing.

2. Merger of Reynolds Brothers with Investing.

A number of breaches of trust were committed by the defendants in connection with the merger of Reynolds Brothers, Incorporated with Investing in 1930. Reynolds Brothers, Incorporated was 80 per cent owned by the defendants Richard S. Reynolds and Clarence K. Reynolds. It had the same officers and directors as Investing, and in addition, the personal attorney of the defendants Richard S. Reynolds and Clarence K. Reynolds. In order to protect the stock interest of the defendants in Reynolds Brothers, Incorporated which was threatened, and in order to obtain a means of collecting through Investing the sums

owed to them by Reynolds Brothers, Incorporated which were uncollectible, the defendants proposed a merger to the stockholders of both corporatons thereof. In connection with the proposed merger, the defendants wrote up the obligation of Reynolds Brothers, Incorporated to them from $340,641 to $425,000. They also inflated the value of the assets of Reynolds Brothers, Incorporated in order to profit personally by receiving a greater number of securities of Investing for their stock in Reynolds Brothers, Incorporated. Knowledge of both these acts was never conveyed to the stockholders of Investing, but on the contrary, the defendants represented to said stockholders that the merger would benefit them. As a result of the merger, the defendants received from Investing a large number of [fol. 30] shares of Investing in excess of the number they should have received and caused Investing to pay to themselves the sum of $425,000 with interest in purported payment of the obligation of $340,641.

3. Syndicate Operations.

The complaint alleges, as further breaches of trust by defendants, that they caused Investing to enter into, take over and retain a number of syndicate participations to the personal profit and benefit of defendants and resulting in substantial losses to Investing.

The preparation of the bill of complaint in this action required extensive examinations, with the aid of accountants, into many complicated and intricate transactions occurring from ten to twelve years prior to the date of their discovery.

In addition, your petitioners' firms cooperated with James D. Carpenter, Jr., one of the plaintiffs, in examinations under 21-A of the Bankruptcy Act held in New Jersey and in Virginia relating to and for the purpose of preparing Action No. 2. In addition to the examination of the factual questions, your petitioners' firms conducted extensive research into a number of questions of law connected therewith.

Issue was joined by the service of the answers of defendants Clarence K. Reynolds and William F. Woodward on December 31, 1940, a time in which your petitioners were actively engaged in the preparation and trial of Action No. 1.

In connection with the preparation of Action No. 2, your petitioners' firms spent 127¼ hours, of which 12 hours were spent by partners and 115¼ hours by associates.

[fol. 31] XVII. Some time after June 21, 1938, when the old Board of Directors of Investing resigned and a new Board, composed of Messrs. Vanderbilt, Stickel, Lynch and Rossi were designated pursuant to the arrangement approved by Judge Fake, your petitioners' firms were advised that Investing had in its possession certain fidelity bonds issued by Globe Indemnity Company covering the acts of its prior directors. Your petitioners were requested to advise the new Board of Directors whether the looting of Investing's treasury in December, 1937 and January, 1938 (forming the basis for Action No. 1) were covered by these fidelity bonds. Your petitioners' firms made an examination of the facts and applicable law and rendered a report to the Board of Directors. In addition, at the instance and request of the Board of Directors, they conferred with officials of the Globe Indemnity Company and others. After Messrs. Gerdes and Carpenter were designated Trustees of Investing pursuant to the order of Judge Fake described above, your petitioners, at the special instance and request of the Trustees prepared for filing with Globe Indemnity Company the appropriate proofs of claim as a condition precedent to the institution of action. On the 16th day of January, 1940, your petitioners' firms commenced an action by the service of a summons on Globe Indemnity Company. On the 6th day of June, 1940, the complaint was duly served. Issue was joined by the service of an answer on September 3, 1940. The case is now at issue. The services of your petitioners' firms in connection with the Globe Action consumed 76 hours, 35 minutes, of which 2 hours, 40 minutes were spent by partners, and 73 hours, 55 minutes by associates.

[fol. 32] XVIII. The foregoing constitutes merely a summary of the nature and extent of your petitioners' services to the plaintiffs in said actions. A more detailed statement of each item of service, together with the time spent thereon and of the disbursements made and necessarily incurred, is annexed hereto as Exhibit A.

XIX. Under the plan of reorganization of Investing, approved, confirmed and consummated, the Company is com-

pelled to keep available $300,00 of its assets to assure payment of expenses incurred in the prosecution of these claims.

XX. On June 3, 1941 your petitioners received from plaintiffs in said actions a letter, a copy of which is annexed hereto marked Exhibit B. In short, said letter advised your petitioners that they were no longer the attorneys for plaintiffs in Action No. 2 and the Globe Action, and that their tenure as attorneys in Action No. 1 was to terminate upon the entry of the judgment after the completion of the reference before Referee Dunn. The discharge of your petitioners was not based upon any claim of petitioners' neglect or wrongdoing, but solely upon the absolute prerogative of a client to change his attorney. In connection with the letter of discharge, plaintiffs asserted that they would request your petitioners to turn over certain materials and memoranda prepared or collected by your petitioners.

Exhibit C is a copy of a letter sent by your petitioners in answer to Exhibit B. Your petitioners stated therein that they would not grant the request until they were [fol. 33] relieved of their responsibilities and their fees and disbursements were paid.

XXI. Thereafter, on June 20, 1941, plaintiffs served upon your petitioners an order to show cause, returnable June 30, 1941, in the Federal District Court for the District of New Jersey, why an order should not be made directing your petitioners to turn over to plaintiffs, as Trustees of Investing, any and all books, papers, records and other data in your petitioners' possession pertaining to "any and all litigation on behalf of the debtor corporation or its Trustees, without prejudice to any motion or application which might be made" by your petitioners, "and to fix the amount of their fees and disbursements." Upon the return day of the motion your petitioners appeared and contested the jurisdiction of the Federal District Court to determine the application of the plaintiffs. Your petitioners' opposition was based upon the contention that since plaintiffs had, with the authority of the Federal Bankruptcy Court, commenced actions in the State Courts of New York, all incidents in connection with said actions, including the nature and extent of petitioners' possessory and charging liens and the enforcement thereof, were exclusively vested in the New York State Court.

After the argument of the motion before Judge Fake, the plaintiffs withdrew their motion upon certain terms and conditions set forth in a stipulation dated July 9, 1941, and "So Ordered" by the Court on or about July 10, 1941, a copy of which is annexed hereto, marked Exhibit D. Paragraph 3 of said stipulation provides that within a reasonable time after the entry of judgment upon the reference, [fol. 34] your petitioners will commence proceedings herein for the fixation of their liens, possessory and charging. It also provides that in conjunction therewith, petitioners will consent to the substitution of attorneys in their place and stead, upon such terms and conditions as this Court may fix. Your petitioners are now in possession of voluminous papers, records, data and other memoranda used or for use in connection with Action No. 1, Action No. 2 and the Globe Action.

Petitioners have received no compensation whatever for the foregoing services. Likewise, the disbursements referred to herein have not been paid.

Wherefore your petitioners pray that an order be made determining the extent of your petitioners' liens, both charging and possessory, in said actions, directing appropriate means for the enforcement thereof and the payment of the amount so determined and for such other and further relief as may be proper.

Dated: December 22, 1941.

Ethelbert Warfield, One of the Above Petitioners.
Lawrence S. Greenbaum, One of the Above Petitioners.

(The foregoing petition was verified December 22, 1941 by Ethelbert Warfield and Lawrence S. Greenbaum.)

[fol. 35] Note re Exhibit "A", Annexed to Petition of B. H. Inness Brown, et al.

This exhibit totaling 134 typewritten pages consisted of a summary statement of services rendered, based on diary entries.

(Omitted pursuant to stipulation.)

EXHIBIT "B", ANNEXED TO PETITION OF B. H. INNESS BROWN, ET AL.

McDermott, Enright & Carpenter

75 Montgomery Street

Jersey City, N. J.

June 3, 1941.

Messrs. Greenbaum, Wolff & Ernst, 285 Madison Avenue, New York, N. Y.

Messrs. Kellogg, Emery & Inness-Brown, 120 Broadway, New York, N. Y.

GENTLEMEN:

Re: Reynolds Investing Company Matters

After mature consideration, we have decided that it is our duty as Trustees to assume the burden ourselves of taking over, preparing and arguing the pending appeals and any additional appeals that may be taken from any judgment that may be entered as a result of the hearings before Referee Dunn. We shall also act directly in the efforts which are being made to collect against C. K. Reynolds, Woodward and others.

There has been consistent and persistent criticism by interested parties because of the duplication of effort in the [fol. 36] past conduct of the litigation. We cannot longer permit two important law firms to have joint charge of this litigation. The situation is obviously anomalous and wasteful. The statute as well as the Plan place the responsibility and control of the litigation in our hands and in the face of the criticism that exists, we feel compelled to take over all pending matters that are in your hands, except the conduct of the hearings before Referee Dunn.

Perhaps we should have done this long ago when the criticism first arose. We recognized however that you had already carefully investigated the facts and prepared the case, and that no savings in expense would result from your displacement prior to the conclusion of the trial. Such reasons no longer prevail, so we shall relieve you henceforth of the burden and responsibility of the litigation. This applies as well to the second cause of action now pending. We doubt that any further time should be put on this

cause of action in New York in view of the questionable responsibility of C. K. Reynolds and Woodward.

We shall expect you to conclude the hearings before Referee Dunn as our attorneys and are confident that you will give us your hearty cooperation in rendering any further service that may seem necessary or desirable. We shall not hesitate to call on you from time to time. We also are confident that you will make available to us any and all materials or memoranda that you may have prepared.

Sincerely yours, (Sgd.) J. Gerdes, James D. Carpenter, Jr., Trustees of Reynolds Investing Company, Inc.

JDC-GCB.

[fol. 37] EXHIBIT "C", ANNEXED TO PETITION OF B. H. INNESS BROWN, ET AL.

Kellogg, Emery & Inness-Brown

120 Broadway

New York

June 4, 1941.

James D. Carpenter, Jr., Esq., and John Gerdes, Esq.,
℅ Messrs. McDermott, Enright & Carpenter, 75 Montgomery Street, Jersey City, N. J.

DEAR SIRS:

This will acknowledge receipt of your letter of June 3.

We have been retained to prosecute these litigations by the corporation and the retention was approved by Judge Fake. Why you should presume to overrule Judge Fake or to assume that your judgment on the question of what you call "duplication" is superior to his, is not clear. In so far as the fact that these litigations are in the joint charge of our two firms is concerned, you are well aware that there never was any intention other than to render a single bill.

It is our view that such duplication as may have existed has been due to the fact that you gentlemen have departed from your functions as clients and have attempted, in many instances without prior notice to us, to act as your own attorneys. However, if, as you assume, there has been any

duplication between the undersigned, we fail to see how such duplication would be decreased by the substitution of the firms of McDermott, Enright & Carpenter and Gerdes [fol. 38] & Montgomery for our firms. In fact any such substitution necessarily requiring the new attorneys to study the record, would really be anomalous and wasteful.

Nevertheless, realizing as we do that your real desire is to take over the additional work necessary to ensure retention of the successes which we have achieved, we are prepared to accede to your wishes, provided:

1. We are relieved of our responsibilities, and

2. Our fees and disbursments to date are paid in full.

Mr. Lawrence S. Greenbaum and Mr. Ethelbert Warfield would be glad to discuss this matter with you. We cannot arrange such a meeting on Saturday but would be glad to meet with you at either ten or eleven o'clock on the morning of Monday, June 9th, at the office of Kellogg, Emery & Inness-Brown. We have chosen that date to accord with Mr. Gerdes' request.

Very truly yours, Kellogg, Emery & Inness-Brown.

CK:fw.

[fol. 39] EXHIBIT "D," ANNEXED TO PETITION OF B. H. INNESS BROWN, et al.

United States District Court, for the District of New Jersey

In Proceedings for Reorganization

In the Matter of REYNOLDS INVESTING COMPANY, INC., a Corporation, Debtor

STIPULATION

It is stipulated by and between the parties hereto as follows:

1. The motion of petitioners, John Gerdes and James D. Carpenter, Jr., returnable before this Court on June 30, 1941, for an order directing respondents Greenbaum, Wolff

& Ernst and Kellogg, Emery & Inness-Brown to turn over certain papers, be and the same hereby is withdrawn.

2. All papers, books, records and other data in respondents' possession pertaining to any and all litigation on behalf of the Debtor or petitioners shall remain in the possession of respondents (a) until the extent of their liens, if any, both charging and possessory, have been determined by the courts of New York, and payment of their fees and disbursements made, if such payment is made a condition for the releasing of such liens, if any; or (b) in the event that it should be finally determined that the courts of the [fol. 40] State of New York shall not make such fixation, then, until a final order of the appropriate court has been entered and complied with by petitioners.

3. Upon conclusion of the reference before Philip Dunn, Esq. in *Gerdes* v. *Reynolds;* et al., and the entry of judgment thereon, the relationship of attorney and client between petitioners and respondents shall terminate, and respondents will within a reasonable time thereafter commence proceedings in the state courts of New York for the fixation of their said liens, if any. Respondents will consent to the substitution of petitioners or other attorneys in place and stead of respondents in all pending actions on behalf of petitioners upon such terms and conditions as shall be fixed by the courts of New York, or if it shall be finally determined that said courts of New York shall not make such fixation and determination of their said liens, if any, then upon such terms and conditions as shall be fixed by the appropriate court and compliance therewith by petitioners.

4. Respondents will provide petitioners with copies of all law memoranda prepared by them not heretofore furnished.

5. Upon reasonable notice at any time, petitioners or such of their employees or associates as are designated by them will be permitted to examine in respondents' offices all exhibits, books, papers, documents or other data relating to the aforesaid litigation and to make copies or photostatic copies thereof; and respondents on reasonable notice, at the expense of the trustees, will produce at any trial or hearing [fol. 41] such exhibits, books, papers, documents or other data in their possession as petitioners may desire to offer in evidence.

6. Nothing in this stipulation or any acts taken hereunder shall constitute an abandonment or waiver in any respect by the respondents of their attorneys' liens, if any, or any other rights which they may possess under the laws of the State of New York, and all such rights are hereby reserved.

7. Nothing herein shall constitute a waiver of the rights of petitioners or respondents to question the jurisdiction of the courts of the State of New York, or the United States District Court for the District of New Jersey, with respect to the determination of the existence, nature or extent of respondents' liens and the payment of their fees and disbursements in connection with the aforesaid litigation.

Dated: New York, July 9th, 1941.

(Sgd.) John Gerdes, James D. Carpenter, Jr., Petitioners. (Sgd.) Greenbaum, Wolff & Ernst, Kel-
[fol. 42] logg, Emery & Inness-Brown, Respondents.

Dated: 10th, 1941.

So ordered.

(Sgd.) Guy L. Fake, United States District Judge.

In Supreme Court of New York, New York County

Answer of Trustees

State of New York,
County of New York, ss:

Answering the petition and application of B. H. Inness-Brown and others in the above-entitled matter, John Gerdes and James D. Carpenter, Jr., as Trustees for Reynolds Investing Company, Inc., Debtor, depose and allege as follows:

1. The applicants were duly appointed attorneys for Reynolds Investing Company, Inc., Debtor, by the United States District Court for the District of New Jersey by order dated August 1, 1938, and were instructed by said Court to bring the action in the New York Supreme Court which is referred to in their petition herein. After the Trustees were appointed in the reorganization proceedings, they were substituted in said New York action in place of

said Debtor, and applicants thereafter, with the approval [fol. 43] of said United States District Court, acted as the attorneys for the Trustees therein. As attorneys for the Debtor and its Trustees, applicants are subject to the exclusive jurisdiction of said United States District Court for the District of New Jersey and said Court has exclusive power to determine the amount of compensation to be paid to them out of the assets in the possession of said Court for services rendered under appointment by said Court.

2. The causes of action which applicants desire this Court to impress with a lien are assets in the possession of the United States District Court for the District of New Jersey and subject to its exclusive jurisdiction. Said United States District Court has never relinquished its possession of said causes of action.

3. The United States District Court for the District of New Jersey, by permitting the amounts of its claims against the defendants in such actions to be liquidated in the New York state courts, did not surrender possession of such causes of action; nor did it consent to the adjudication by the New York courts of claims or liens which might be asserted by applicants or others against such causes of action.

4. Applicants have never applied for, or received, permission from said United States District Court to use the New York courts to establish liens against said causes of action.

5. In accepting appointment by the United States District Court for the District of New Jersey to act as attorneys for the Debtor, and subsequently for its trustees, in reorganiza- [fol. 44] tion proceedings under Chapter X of the Federal Bankruptcy Act, applicants agreed that the amounts of their compensation should be determined by said Court. They further agreed that all statutes and Court rules regulating applications by attorneys for allowances for services in connection with the administration of estates under Section 77B or Chapter X of the Bankruptcy Act, should be applicable to them.

6. After their appointment, and at various times during and after the month of November, 1939, applicants agreed that the United States District Court for the District of New Jersey should fix the reasonable compensation to be

paid to them for the services which they now ask the New York courts to value.

7. The applicants constituting the firm of Greenbaum, Wolff & Ernst were the attorneys for the Langmuir Debenture Holders Committee in the reorganization proceedings of Reynolds Investing Company, Inc., Debtor, under Chapter X of the Bankruptcy Act, in the United States District Court for the District of New Jersey, until they were superseded in or about the month of October, 1940. They have been paid, by order of said United States District Court, the sum of $21,000 for their services and $1,305.79 for their disbursements as attorneys for said Committee.

8. The applicants constituting the firm of Kellogg, Emery & Inness-Brown were, and still are, the attorneys for the Dochez Preferred Stockholders Committee in said reorganization proceedings, and have been paid, by order of said United States District Court, the sum of $15,000 for [fol. 45] their services and $709.90 for their disbursements as attorneys for said Committee.

9. The applicants were originally appointed as attorneys for the Debtor to prosecute the actions in this Court, and were subsequently continued as attorneys therein for the Trustees, because they were the attorneys for the aforesaid Committees, which were the principal and dominating committees in the aforesaid reorganization proceeding.

10. On or about October 28, 1939 the Trustees proposed a plan of reorganization in said proceeding which contained the following provisions (italics and words in brackets supplied by us):

"V. Recognition of the Interests of Creditors and Stockholders in the Plan

"The plan contemplates that all reorganization debts and expenses, and all claims of creditors other than claims on old debentures, as finally allowed by the Court, will be paid immediately in full in cash."

"XI. Reservation of Claims

"All claims in favor of the Debtor or of the Debtor's estate not settled or adjusted in the reorganization proceed-

ings, or in the plan, or in connection with the consummation of the plan, shall be retained and enforced by the Trustees. The Company shall cooperate with and assist the [fol. 46] Trustees in every way in the prosecution and collection of such claims.

"The Trustees shall have full power to prosecute pending actions and proceedings involving such claims, and to bring additional actions or proceedings in the courts of any jurisdiction. They shall also have full power to employ, retain, or displace, attorneys or counsel representing them in any action or proceeding, whether such action or proceeding be pending at the time of the consummation of the plan or not. They shall not, however, have any power to discontinue, compromise or settle any action or proceeding without the express approval of the Court.

"The Court will retain continuing jurisdiction over such claims and the prosecution thereof, and over the Company, its books, records and papers, and the Trustees, in connection therewith, after the final decree in the reorganization proceedings. *The Court* [the United States District Court for the District of New Jersey] *will from time to time fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of such claims*, and the Company shall assume and pay the amount of such compensation as well as all other expenses incurred or paid by the Trustees in the prosecution, collection, or other disposition of the claims. If the value of the portfolio of the Company shall, at any time prior to a complete and final adjudication on the merits of all of the claims reserved to the Trustees, be $300,000 or less, the as- [fol. 47] sets of the Company shall not be further depleted by purchases or redemption of debentures or shares of preferred stock without order of the Court after a hearing upon notice to the Trustees. In such order the Court will specify the financial arrangements to be made by the Company for the payment of all expenses then already incurred in connection with the claims as well as such other expenses as may reasonably be necessary in the further prosecution thereof.

"The net proceeds ultimately resulting from the prosecution or other disposition of the claims will be paid to the Company."

"XIII. Approval, Acceptance, Confirmation and Consummation of the Plan.

"All costs and expenses of administration and all allowances which may be approved or made by the Judge, shall be paid in cash by the Trustees, or, after the consummation of the plan, by the Company."

"The Court shall retain jurisdiction over the assets dealt with in the plan, and over any and all persons, firms, or corporations to whom such assets may be transferred, and over all parties appearing in the reorganization proceedings, for the purpose of carrying out and giving effect to any and all provisions of the plan and the decree confirming the same."

11. Applicants approved the aforesaid provisions in or about the month of November, 1939, and have at all times [fol. 48] since said date approved similar provisions in revisions of said plan. They have, from time to time, urged the Court, the holders of debentures and shares of preferred stock and other interested parties, to approve and accept plans containing such provisions. They have never, directly or indirectly, expressed disapproval or lack of acquiescence with respect to the aforesaid provisions.

12. The plan which was finally confirmed and actually consummated in 1940 with the active support of applicants, contains the provisions quoted in paragraph 10 hereof. A copy of said plan is annexed hereto as Exhibit A.

13. The claim of applicants for compensation for the services set forth in their application is a reorganization debt and expense.

14. All of the services of applicants described in their petition and application herein were services in the prosecution of claims as to which the United States District Court retained jurisdiction in the provisions of the plan which are referred to in paragraphs 10 and 12 hereof.

15. After their appointment by the United States District Court for the District of New Jersey as attorneys for the Debtor to institute the action in which applicants rendered the services for which they seek compensation, said applicants, as attorneys for the Langmuir Debenture Holders Committee and the Dochez Preferred Stockholders

Committee, united with the attorneys for other interested parties in the preparation and submission to the United [fol. 49] States District Court of the order made and entered January 19, 1939 by said Court appointing deponents as Trustees. A copy of said order is annexed hereto as Exhibit B.

16. Applicants acquiesced and consented to all of the provisions of the order of the United States District Court for the District of New Jersey, dated June 17, 1940, which confirmed the plan of reorganization. A copy of said order is annexed hereto as Exhibit C.

17. No final decree has been signed or entered in the reorganization proceedings in the United States District Court for the District of New Jersey.

18. The United States District Court for the District of New Jersey and its Trustees in the reorganization proceedings have not at any time consented to the institution of this proceeding in the New York court, or to any other proceeding to enforce any lien upon the estate of the Debtor. No application has been made to said Court or its Trustees for permission to make the pending application.

19. Applicants have not complied with Section 62(d) and 247 of the Bankruptcy Act, and the procedure adopted by petitioners herein; and the papers submitted by them on this application, do not comply with the statutes and court rules regulating applications of attorneys for allowances for services in connection with the administration of corporations in reorganization proceedings under section 77B or Chapter X of the Bankruptcy Act.

[fol. 50] 20. Applicants and the Trustees have agreed that only facts bearing on the jurisdiction of the Court be submitted at this time. This affidavit is therfore limited to such facts.

21. The Trustees respectfully ask that this application be denied and that applicants be referred to the United States District Court for the District of New Jersey for a determination of the value of their claims and the enforcement of any liens which they may have.

John Gerdes, James D. Carpenter, Jr.

(Sworn to January 12, 1942.)

Exhibit "A", Annexed to Answer of Trustees

Plan of Reorganization

District Court of the United States,
For the District of New Jersey

In the Matter of Reynolds Investing Company, Inc., a Corporation, Debtor

In Proceedings for Reorganization

I. Nature of Proposed Plan

The plan of the Trustees proposes a complete liquidation of the assets of the Debtor under the control of the holders [fol. 51] of the old debentures, and a distribution of the proceeds of such liquidation among the holders of the old debentures, old preferred stock and old common stock according to their strict legal priorities.

The maturity date of the debentures will be April 1, 1946, instead of April 1, 1948, but it is contemplated that most or all of such debentures will be retired by purchase or redemption prior to 1946. Interest will continue to be payable semi-annually at the rate of 5% per annum.

No dividends are to be paid, and no shares of stock of any class are to be retired by redemption, until all the debentures shall have been paid or retired.

Holders of old preferred stock are to receive a distribution of $145 per share before any payment is to be made to holders of old common stock.

There is to be a dissolution of the Company on April 1, 1946, unless all of the debentures and shares of preferred stock shall have been paid or retired before such date. Even if all the debentures and preferred stock shall then have been paid or retired, the Company will be dissolved unless the holders of a majority of the shares of common stock shall vote against dissolution.

As the reorganized Debtor is not to operate as an active investment trust, its name is to be changed to "Reynolds Realization Corporation".

The plan proposes liquidation through the medium of a reorganized Debtor rather than through an adjudication in bankruptcy, because: (1) the extent of the solvency of the Debtor is uncertain, and a judicial determination of the

extent of such solvency would involve protracted litigation, [fol. 52] litigation, be expensive, and, in the end, be useless; (2) complete and satisfactory liquidation is a practical impossibility within the time ordinarily contemplated by bankruptcy or other liquidation through legal proceedings; (3) corporate management is more flexible and better able to meet unforeseen contingencies in a liquidation over a long period of time than is the case where the liquidation is managed by officers of a court; and (4) control of a liquidation which necessarily extends over a long period of time should be under the direct and immediate control of those primarily interested—the debenture holders and stock owners.

II. Present Financial Condition of Debtor

A. *Assets*

The principal assets of the Debtor (excluding cash balances aggregating approximately $30,000 on September 30, 1939) consist of:

(1) Causes of action in favor of the Debtor against its former officers and directors;

(2) Securities readily marketable; and

(3) Securities having no ready market or a market so thin that the holdings of the Debtor may not be sold within a reasonable period of time in the market.

The causes of action in favor of the Debtor are in a face amount in excess of $3,000,000. No accurate value can be placed upon these claims at this time.

The readily marketable securities had a market value of $1,048,155.50 as of January 19, 1939, and $1,083,341.50 as of September 30, 1939.

[fol. 53] The securities listed as being "not readily marketable" in the report of the Trustees dated August 8, 1939 (see Appendix C, Report, p. 67) were appraised by the Trustees as having a value of $2,026,703.77 as of January 19, 1939; on the same date, the nominal market value of these securities was $2,031,226.06 (including the Class A shares of the United States Foil Co., on which there are no market quotations, at $2 per share more than the market value of the Class B shares of the same corporation). These securi-

ties had a nominal market value of $1,996, 001.75 as of September 30, 1939.

B. *Outstanding Obligations and Stock*

The capital and debt structure of the Debtor is comparatively simple.

Claims against the Debtor aggregating $36,974.55 have been filed by creditors other than holders of old debentures. The validity of most of these claims is being disputed by the Trustees.

$3,439,900 in principal amount of old debentures, due April 1, 1948, and bearing interest at 5% per annum, are outstanding. No default has occurred in the payment of interest on these debentures. Interest up to and including October 1, 1939 has been paid. The April 1, 1940 interest will be paid, as authorized by court order.

There are 9,915 shares of old no par value $6 cumulative preferred stock outstanding which are entitled to $100 per share, plus unpaid cumulative dividends, in the event of involuntary liquidation. As of January 1, 1940, $45 per share of unpaid dividends will have accumulated. As of such date, therefore, or of any date prior to July 1, 1940, each share of [fol. 54] old preferred stock will be entitled, in an involuntary liquidation, to $145 in priority to any distribution to holders of shares of old common stock. (The plan gives a priority of $145 to shares of preferred stock because it is estimated that the plan will be confirmed after January 1, 1940, and prior to July 1, 1940.)

There are 1,787,859 shares of old $1 par value common stock outstanding, including shares reserved to exchange for old shares, scrip, and Reynolds Brothers Incorporated stock.

III. Definition of Terms

Each of the following terms when used herein shall have the meaning specified respectively unless a different meaning is clearly indicated by the context:

(1) *Debtor or Company:* Reynolds Investing Company, Inc., a Delaware corporation, the name of which is to be changed to "Reynolds Realization Corporation" upon the consummation of the plan.

(2) *Reorganization Proceedings:* The proceedings for the reorganization of the Debtor now pending under Chapter X of the Bankruptcy Act, in the United States District

Court for the District of New Jersey, entitled "In the Matter of Reynolds Investing Company, Inc., a Corporation, Debtor—In Proceedings for Reorganization."

(3) *Court:* The District Court of the United States for the District of New Jersey, or any judge or referee in bankruptcy, acting in the reorganization proceedings.

[fol. 55] (4) *Trustees:* John Gerdes and James D. Carpenter, Jr., as trustees of the Debtor in the reorganization proceedings, and their successor or successors, if any.

(5) *Plan:* This plan of reorganization and any modifications thereof.

(6) *Old Debentures:* The outstanding Twenty-Year 5% Gold Debentures, Series A, of the Debtor, due April 1, 1948, excluding debentures owned by the Debtor or the Trustees.

(7) *Debentures* or *New Debentures:* The old debentures modified as provided in this plan.

(8) *Old Trust Indenture:* The trust indenture dated as of April 1, 1928, between the Debtor and The Seaboard National Bank of the City of New York as trustee, and an indenture supplemental thereto dated July 1, 1928, under and pursuant to which the old debentures were issued.

(9) *Trust Indentre* or *New Trust Indenture:* The old trust indenture modified as provided in this plan.

(10) *Indenture Trustee:* The Commercial National Bank and Trust Company of New York, or its successor, as trustee under the trust indenture or the old trust indenture.

(11) *Old Preferred Stock:* The outstanding shares of cumulative $6 preferred stock without par value, of the Debtor, excluding shares owned by the Debtor or the Trustees.

(12) *Preferred Stock* or *New Preferred Stock:* The preferred stock of $10 par value, entitled in voluntary or involuntary liquidation to $145 per share, to be issued pursuant to the plan.

[fol. 56] (13) *Old Common Stock:* The outstanding shares of $1 par value common stock of the Debtor, excluding shares owned by the Debtor or the Trustees but including shares held or reserved to exchange for old shares, outstanding scrip certificates or shares of the capital stock of Reynolds Brothers Incorporated.

(14) *Common Stock* or *New Common Stock:* The common stock of 50¢ par value to be issued pursuant to the plan.

(15) *Voting Trust Agreement:* The voting trust agreement under which the shares of new preferred stock and new common stock are to be deposited in accordance with the terms of the plan.

(16) *Voting Trustees:* The persons designated as voting trustees in the voting trust agreement, and their successor or successors.

(17) *Class A Voting Trust Certificates:* The certificates, issued by the Voting Trustees pursuant to the voting trust agreement, which represent ownership interests in shares of preferred stock.

(18) *Class B Voting Trust Certificates:* The certificates, issued by the Voting Trustees pursuant to the voting trust agreement, which represent ownership interests in shares of common stock.

(19) *Value of the Portfolio:* The value of such securities owned by this Company (excluding its own issues and voting trust certificates representing such issues) as have an "over the counter" or other general market. The price of the last sale, or, in the absence of a sale, the last bid quotation, [fol. 57] shall be used to determine such value. All securities on which there shall have been no public sales or bid quotations within the preceding 30 days shall be eliminated in the calculation of the value of the portfolio, except that Class A shares of United States Foil shall, in the absence of public sales or quotations, be valued at $2 per share in excess of the market value of Class B shares of United States Foil.

(20) *Asset Value of Debentures:* The asset value of $1 of debentures shall be determined by deducting all the liabilities of the Company (excluding capital stock, surplus and debentures) from the cash on hand and the value of the portfolio of the Company, and then dividing the remainder by the amount of outstanding debentures.

(21) *Asset Value of Preferred Stock:* The asset value of each share of preferred stock shall be determined by deducting all the liabilities of the Company (including the principal and unpaid accrued interest on outstanding Debentures but excluding capital stock and surplus) from the cash on

hand and the value of the portfolio of the Company, and then dividing the remainder by the number of the outstanding shares of preferred stock.

IV. Proposed Recapitalization

The reorganized Company will have the following capitalization:

$3,439,900, principal amount, of 5% debentures, maturing April 1, 1946.

[fol. 58] 9,915 shares new preferred stock of $10 par value, entitled in voluntary or involuntary liquidation to $145 per share.

178,786 shares new common stock of 50¢ par value.

V. Recognition of the Interests or Creditors and Stockholders in the Plan

The plan contemplates that all reorganization debts and expenses, and all claims of creditors other than claims on old debentures, as finally allowed by the Court, will be paid immediately in full in cash.

Each holder of old debentures will receive an equal amount of new debentures.

The 9,915 shares of new preferred stock and the 178,786 shares of new common stock will be issued to voting trustees under a voting trust agreement which is more fully hereinafter described.

Each holder of shares of old preferred stock will receive a Class A certificate from the Voting Trustees giving ownership rights (except the right to vote) in an equal number of shares of new preferred stock. Such shares of new preferred stock will entitle the owners, to the extent to which the amount realized upon the liquidation of the assets of the Company leaves a surplus after payment in full of the claims of creditors and debenture holders, to receive $145 in cash for each share of preferred stock before any payment is made to any of the holders of common stock or of trust certificates representing shares of old common stock.

Each holder of shares of old common stock will receive [fol. 59] a Class B certificate from the Voting Trustees giving ownership rights (except the right to vote) in shares of new common stock in the proportion of one share of new common stock for each ten shares of old common stock.

These certificates will entitle the holders to their proportion of the net amount recovered upon the liquidation of all the assets of the Company after payment in full of the claims of creditors, debenture holders and holders of preferred stock, if a majority of the Class B certificate holders shall vote to dissolve the Company. If dissolution shall not be voted, holders of Class B certificates shall be entitled to the shares of the new common stock represented by their certificates.

If the plan is not accepted in writing by or on behalf of stockholders holding a majority of the shares of stock of which proofs have been filed and allowed, of any class, then in lieu of the provisions made herein for such class, adequate protection for the realization by them of the value of their equity, if any, in the property of the Debtor will be provided by appraisal by the Court and payment in cash of the value of their stock.

No such provision is made for the realization by the old debenture holders (which is the only class of creditors affected by the plan) of the value of their claims against the property dealt with by the plan and affected by their claims, for the reason that the acceptance of the plan by two-thirds of the old debenture holders who file individual proofs of claim and whose claims are allowed is essential to the confirmation of the plan.

[fol 60] VI. Management and Control

A. *Composition of Board of Directors*

The reorganized Company shall be managed by a board of directors of five members who shall exercise their powers subject to such restrictions and qualifications as may be set forth in the by-laws, the certificate of incorporation, and the trust indenture covering debentures.

The members of the board of directors during the first year following the consummation of the plan shall be as follows:

	NAME
Debenture Representatives	Dean Langmuir
Preferred Stock Representative	G. Vernor Rogers
Common Stock Representative	Samuel S. Rodman
	Richardson Morris
	Edwin H. Woarms

The foregoing directors shall serve until the annual meeting of the Company in 1941 and until the election and qualification of their successors.

B. *Election of Officers*

Immediately following their taking of office hereunder, the first board of directors shall elect a president, a vice-president, a secretary, and a treasurer, and such other officers as the by-laws may prescribe, to serve at the pleasure of said board of directors until the annual meeting of the [fol. 61] Company in 1941 and the election and qualification of their successors.

C. *Election of Directors*

At the annual meeting of the Company in 1941, and thereafter, the holders of new debentures shall have the right, to the exclusion of the holders of the preferred and common stoock, to elect three of the five directors of the company until the asset value of the outstanding debentures shall be more than 200% of the amount of principal and unpaid cumulated interest thereof and the principal amount of outstanding debentures shall be less than $750,000; in such event, and until all of the debentures shall have been paid or retired, the holders of debentures shall be entitled to elect two of the directors. The right of the holders of debentures to elect three directors shall again become effective from time to time whenever the asset value of the outstanding debentures shall be less than 200% of the amount of the principal and unpaid interest of such outstanding debentures, or if $500,000 in face amount of debentures shall not have been retired by purchase or redemption in the preceding calendar year.

Whenever the holders of debentures shall have the right to elect three directors, the holders of the preferred stock shall have the right to elect one director. When the holders of debentures shall be entitled to elect only two directors, the holders of preferred stock shall have the right to elect two directors. After all debentures shall have been retired by purchase or redemption, the holders of preferred stock shall have the right to elect three directors.

[fol. 62] So long as any debentures are outstanding, the holders of common stock shall be entitled to elect one director. After the retirement of all debentures by purchase

or redemption, and until all of the preferred stock shall have been retired by purchase or redemption, the holders of common stock shall have the right to elect two directors; thereafter all directors shall be elected by vote of the holders of common stock.

The rights of holders of debentures, preferred stock and common stock to elect directors shall be determined by the facts existing at the close of the preceding calendar year.

D. *Voting by Holders of Debentures*

Only registered owners of debentures shall be entitled to vote.

At elections of directors of the Company each holder of debentures shall be entitled to one vote for each $100 principal amount of debentures held by him multiplied by the number of directors to be elected by the holders of debentures and he may cast all of such votes for a single director, or may distribute them among the number to be voted for by debenture holders, or any two or more of them, as he may see fit. At other meetings at which the debenture holders may be entitled to vote, each holder of a debenture shall be entitled to one vote for each $100 principal amount of debentures held by him.

Holders of debentures may vote by proxy in manner similar to the voting by proxy of holders of shares of stock.

E. *Quorums at Meetings*

At all meetings, holders of debentures, shares of preferred stock and shares of common stock, shall vote as separate [fol. 63] classes. The presence, in person or by proxy, of the holders of at least 25% of the number or principal amount, respectively, of the outstanding shares or debentures of each class shall be required to constitute a quorum of such class, and such quorum shall be sufficient to take the action which the holders of such shares or debentures are entitled to take, whether or not a quorum of the holders of the other classes of such securities shall be present. In the absence of a quorum of any class of securities, a majority of the holders of such class of securities present shall have the power to adjourn the meeting from time to time, without notice other than announcement at the meeting, until the holders of the requisite number or amount of such class of securities shall be present in person or by proxy.

F. Vacancies in Board of Directors

If any vacancy shall occur among the representatives of any class of securities on the board of directors, such vacancy shall be filled by vote of the holders of the securities of such class.

G. Compensation to Officers, Directors and Employees

The board of directors shall fix all salaries and compensation to officers, directors and employees. No officer or director shall, however, in either or both capacities receive compensation in excess of $2,000 per annum unless he shall devote all of his time to the affairs of the Company; and no officer, director or employee, devoting all of his time to the affairs of the Company, shall receive compensation [fol. 64] in excess of $3,000, per annum. The holders of debentures may by vote, at a meeting upon due notice, authorize the payment of compensation in excess of the foregoing amounts.

VII. Limitations Upon Management

A. Sales of Securities

Except as otherwise provided in the following paragraphs hereof, the power of the board of directors to authorize the sale of securities shall be unrestricted.

The preferred and common shares of Stokely Brothers & Co., the common shares of Case, Pomeroy & Co., and the Class A shares of United States Foil Co., or any part of such shares, shall be sold only, (1) when the sale is authorized by the affirmative vote of four directors; or (2) when the sale of such shares, in whole or in part, is authorized by the affirmative vote of three directors at the following, or better, prices:

Stokely Bros. & Co., Common	$ 7⅞ per share
Stokely Bros. & Co., Convertible Preferred	18¾ per share
Case, Pomeroy & Co., Common	15 per share
United States Foil Co., Class A	14.34 per share

The foregoing prices shall in each case be diminished by an amount equal to the total of all dividends designated as "liquidating dividends" which may have been received after the date of this plan and prior to the sale of the shares.

Whenever any security in the portfolio of the Company (other than the preferred and common shares of Stokely [fol. 65] Brothers & Co., the common shares of Case, Pomeroy & Co., and the Class A shares of United States Foil Co.) shall have a market value, per bond or per share, of 125% or more of its value as of January 19, 1939, as appraised in the Trustees' report of August 8, 1939, the board of directors shall be required to take reasonable steps to sell such number of the bonds or shares, at such value of 125% or more, as will reduce the Company's holding to not more than 75% of the number of such bonds or shares held on January 19, 1939. When the market value reaches 150%, the Company's holding shall be reduced to 50% of its holding on January 19, 1939. Similarly, the holding shall be reduced to 25% when the market value reaches 175%, and be completely liquidated when a price of 200% of such value, or more, can be secured.

B. Investment of Funds

Investments of funds shall not be made except in securities of the Company, and investments in securities of the Company shall be made only as expressly authorized in this plan.

C. Loans to the Company

So long as any debentures or shares of preferred stock are outstanding, the Company shall not borrow money to purchase its own debentures or shares of stock or to pay for other investments or securities, and shall not at any time have outstanding loans aggregating more than $85,000, exclusive of debentures.

[fol. 66] VIII. Provisions as to Debentures

A. General

Subject to prior retirement by purchase or redemption, the principal of the debentures shall become due April 1, 1946. Interest at the present rate of 5% per annum, shall be payable every six months.

No "touch off" clause requiring the Company to redeem all of its outstanding debentures when its assets are less than a given percentage of its funded debt, shall be applicable to the new debentures, but upon the happening of

any of the following defaults by the Company, the Indenture Trustee shall be permitted to issue a declaration of default which shall cause the principal of all outstanding debentures to become due and payable immediately: (a) failure to pay interest on the debentures; (b) failure to take reasonable steps to sell securities as required by the last paragraph of division A of article VII of the plan; (c) violation of the provisions of division B of article VII of the plan as to investments; (d) borrowing money in violation of the provisions of division C of article VII of the plan; (e) failure to retire the required number of debentures or to have the cash or United States Government securities on hand to cover such debentures, as required by division D of article VIII of the plan; (f) failure to observe the prohibition upon the declaration or payment of dividends on any class of stock, or upon the purchase of Class B voting trust certificates representing shares of common stock, as set forth in the second paragraph of division A of article IX of the plan; and (g) failure to observe the conditions under which shares of preferred [fol. 67] stock may be purchased or redeemed, as set forth in divisions B and C of article IX of the plan. Written notice of a declaration of default shall be given by the Indenture Trustee to the Voting Trustees and to all holders of debentures, by mail. Notice by mail of a declaration of default shall be given promptly by the Voting Trustees to all holders of Class A and Class B voting trust certificates.

The Indenture Trustee shall give thirty days notice in writing by mail to the Company, and to the Voting Trustees and all holders of debentures, of any claim of default, and an opportunity to the Company during such period of correcting such default, before it shall issue its declaration of default, except as to the following defaults, as to which the Indenture Trustee shall issue a declaration of default without prior notice and without an opportunity to the Company of correction: (a) investment other than in securities of the Company; (b) borrowing money in excess of $85,000; (c) purchase or redemption of Class A voting trust certificates or shares of preferred stock before the retirement of all debentures; (d) purchase of Class B voting trust certificates; and (e) payment of any dividend on either the preferred or common stock. The Voting Trustee shall promptly mail notice of a claim of default to all holders of Class A and Class B voting trust certificates.

All debentures shall be registered.

The names and addresses of holders of debentures, and of the amount of debentures held by them respectively, shall be registered by the Company in a record kept at the places at which the Company's stock ledgers are kept and shall be open to the examination of every debentureholder and stockholder at the times and in the manner provided for the [fol. 68] examination of its stock ledgers by stockholders.

Holders of debentures shall have the same right of inspection of the books, accounts and records of the Company, including stock ledgers, and shall have all the other rights, which stockholders have or may have by reason of the provisions of the certificate of incorporation of this Company as amended or of the statutes of Delaware or any other state in which the Company does business.

The certificate of incorporation shall be amended only when the amendments have been approved by the affirmative vote of the holders of at least 75% of the principal amount of the debentures then outstanding and voting.

B. Purchase and Cancellation

When interest payment checks are mailed on or about the first days of April and October in each year to the registered owners of debentures, a notice shall be enclosed to the effect that holders may at any time tender their debentures for sale to the Company at a price not exceeding the redemption price. The notice shall state the asset value of the debentures as of a date within 10 days prior to the date of the notice, and shall also state that the tender must set forth the amount of debentures offered, the price or prices which will be acceptable, and that the tender will be good for a period of six months or such shorter period as may be specified. A form on which the tender may be made shall accompany the notice.

The Company may from time to time purchase debentures for cancellation, provided that it shall not pay for such [fol. 69] debentures more than the lowest of the following amounts: (1) the par amount of such debentures with accrued and unpaid interest; (2) 80% of the asset value of such debentures; (3) the price at which debentures may be purchased in the market; and (4) the price at which debentures may be purchased under unexpired tenders filed with the Company. Where the prices are the same, deben-

to debentures purchasable in the market.
tures offered upon tender shall be purchased in preference

C. Redemption

The Company shall have the right, from time to time, on any semi-annual interest payment date, to take up and pay any or all of the debentures then outstanding by paying the principal thereof with all interest accrued and unpaid to the date so fixed for prepayment. If only part of the outstanding debentures are to be redeemed, the debentures to be redeemed shall be determined by lot under the direction of the Indenture Trustee. The Company shall give written notice of its election to prepay all or any of the debentures to the Indenture Trustee at least thirty days prior to the day fixed for such prepayment. The Indenture Trustee shall mail, at least two weeks prior to the date fixed for prepayment, a notice in writing to the registered owner of each debenture called for prepayment, which notice shall contain the number and amount of the debenture which has been called and shall state that upon presentation of such debenture for cancellation at the office of the Indenture Trustee 100% of the principal of such debenture, with all unpaid accrued interest thereon, will be paid to the owner. [fol. 70] On or before the date fixed for payment, the Company shall deposit with the Indenture Trustee to the credit of the owner of each debenture called for redemption a sum of money equal to the principal and unpaid accrued interest thereon to the date fixed for redemption, which deposit shall operate as full payment of the debenture as between the Company and the owner thereof. Such deposits in the hands of the Indenture Trustee shall draw no interest. The owner shall look for payment of the debenture and interest thereon only to the sum so deposited in the hands of the Indenture Trustee, and in no event to the Company. The sum so deposited shall be paid by the Indenture Trustee to the owner thereof upon the presentation and delivery to it of the debenture with properly executed instruments of assignment or cancellation.

Any and all debentures paid and delivered as aforesaid shall be cancelled immediately by the Indenture Trustee and delivered so cancelled to the Company.

The right of the Company to redeem debentures, as herein provided, shall not be exercised unless the Company is unable to purchase the debentures in the open market or else-

where at the redemption price or less; nor shall such redemption right be exercised at any time as to less than all the outstanding debentures when the asset value of the outstanding debentures shall be less than 125% of the principal and unpaid accrued interest of such outstanding debentures.

D. Compulsory Retirement

On or before April 1, 1941, the Company shall (by purchase, redemption, or otherwise) retire at least $350,000 [fol. 71] in principal amount of its debentures; it shall retire at least $900,000 in principal amount of debentures on or before April 1, 1942; and on or before April 1, 1943, it shall retire a sufficient number of its debentures to leave outstanding on said date a total principal amount of not more than $1,719,950 of such debentures. By April 1, 1945, the outstanding debentures shall be reduced to $687,980, or less, in principal amount. If on any of said dates the outstanding and unretired debentures shall be in excess of the principal amounts which would have been outstanding and unretired if the foregoing retirements had been made, the Company shall not be in default if it shall then have on hand United States Government securities and cash in an amount equal to the principal and accrued interest on the outstanding debentures in excess of such amounts. In such event, sufficient in amount of Government securities and cash shall be set aside to enable the purchase or redemption of the necessary amount of debentures. Securities and cash so set aside shall be used for no other purpose.

IX. Provisions as to Preferred Stock

A. General

The shares of preferred stock shall have a par value of $10 per share. The holders thereof shall be entitled, in the event of redemption, or voluntary or involuntary dissolution or liquidation, to $145 per share before any sum shall bet paid to or any assets distributed among the holders of the common stock. They shall also have the voting rights elsewhere set forth in this plan. In all other respects the rights and privileges of holders of preferred stock shall [fol. 72] be the same as those of the holders of common stock.

No dividends shall be paid on the shares of any class of stock of the Company until all of its debentures and shares of preferred stock shall have been paid, cancelled or retired. No shares of common stock and no voting trust certificates representing such shares shall be purchased by the Company until after the payment, cancellation or retirement of all debentures and shares of preferred stock. Shares of preferred stock and voting trust certificates representing such shares shall not be purchased or redeemed except as hereinafter provided.

B. Purchase of Class A Voting Trust Certificates

Whenever all of the debentures shall have been paid, cancelled or retired, the Company may from time to time purchase Class A voting trust certificates representing shares of its preferred stock, provided that the purchase price of such Class A voting trust certificates shall not be greater than the lowest of the following amounts: (1) $145 for each share of preferred stock represented by the certificates purchased; (2) 80% of the asset value of the shares represented by the certificates; (3) the prices at which such Class A voting trust certificates may be purchased in the market; and (4) the prices at which such Class A voting trust certificate may be purchased under unexpired tenders filed with the Company. Where the prices are the same, Class A certificates offered upon tender shall be purchased in preference to certificates purchasable in the market.

After all of the debentures shall have been retired, the Company shall mail to the registered owner of each Class [fol. 73] A voting trust certificate a notice to the effect that he may at any time tender all the shares represented by his certificate, or any part thereof, for sale to the Company at a price not exceeding $145 for each share of preferred stock. Semi-annually thereafter, similar notices shall be mailed. The notice shall state the asset value of each share of the outstanding preferred stock as of a date within 10 days prior to the date of the notice, and shall also state that the tender must set forth the number of shares represented by the certificates offered, the price or prices which will be acceptable, and that the tender will be good for a period of six months or such shorter period as may be specified. A form on which the tender may be made shall

accompany the notice. No purchase of Class A voting trust certificates shall be made by the Company at any time unless a notice similar to the foregoing shall have been mailed within seven months immediately preceding such purchase.

All Class A voting trust certificates purchased or otherwise acquired by the Company shall be surrendered to the Voting Trustees for cancellation. Upon receipt of such certificates the Voting Trustees shall transfer to the Company, for retirement, the shares of preferred stock represented by the Class A certificates surrenderd.

C. Redemption of Preferred Stock

The Company shall have the right, from time to time, to redeem any or all of the shares of preferred stock represented by Class A voting trust certificates, by paying the sum of $145 for each share of preferred stock called for redemption. If only part of the outstanding shares of preferred stock are to be redeemed, the shares to be re- [fol. 74] deemed, and the voting trust certificates representing such shares, shall be determined by lot under the direction of the board of directors. The Company shall give at least 30 days written notice to the Voting Trustees of its election to redeem such shares, and shall mail, at least two weeks prior to the date fixed for redemption, a notice in writing to each registered owner of a Class A voting trust certificate which represents shares called for redemption. Such notice to the certificate holder shall specify the number of shares of preferred stock represented by his voting trust certificate which have been called for redemption and state that upon presentation of his voting trust certificate at the office of the Company, on or after the date fixed for redemption, the sum of $145 will be paid for each share called for redemption. When some but not all of the shares of preferred stock represented by a voting trust certificate are called for redemption, payment shall be made for the shares to be redeemed and a new voting trust certificate shall be issued by the Voting Trustees for the shares not called for redemption.

The shares called for redemption, and the Class A voting trust certificate representing such shares, shall not be deemed to be outstanding for any purpose whatsoever from and after the date fixed for redemption, and the rights of the holders of the Class A voting trust certificates representing

shares called for redemption shall be limited solely to the right to receive payment of the sum of $145 for each share called for redemption and a new voting trust certificate for the shares not called for redemption.

At its election the Company, prior to the date fixed for redemption, may deposit the sum of $145 for each share [fol. 75] of preferred stock called for redemption, in trust for the holders of the Class A voting trust certificates representing such shares, with a bank or trust company doing business in the City of New York, and having a capital, surplus and undivided profits of at least $5,000,000. In such case the redemption notice shall (a) state that such deposit has been made, (b) specify such bank or trust company as the place of payment of the redemption price, and (c) call upon the certificate holders to surrender the certificates representing such of the shares as have been called for redemption on or after the redemption date fixed in the notice.

There shall be no redemption of shares of preferred stock while any debentures are outstanding; nor, as to less than all the outstanding shares of preferred stock, when the asset value of each share of preferred stock shall be less than $185; nor unless the Company shall be unable to purchase Class A voting trust certificates in the open market or elsewhere for $145 or less for each share represented.

X. Provisions as to Voting Trust

All of the shares of the new preferred and common stock shall be deposited with Arthur T. Vanderbilt and Charles F. Lynch, as Voting Trustees, under a trust agreement containing appropriate terms to give effect to all of the provisions of this plan. In addition to such terms, the voting trust agreement shall continue the following specific provisions:

(1) The Voting Trustees shall vote all deposited shares.

[fol. 76] (2) The Voting Trustees, upon receipt of certificates of shares of the old preferred and common stock with proper proof of ownership, shall issue to each owner of old preferred stock a Class A voting trust certificate representing an equal number of the shares of the new preferred stock, and to each holder of old common stock a Class B

voting trust certificate representing one share of new common stock for each ten shares of old common stock.

(3) The Voting Trustees shall arrange for separate meetings of the holders of Class A and Class B certificates to be held prior to the annual stockholders' meetings of the Company in 1941, and thereafter. At such meetings the Class A certificate holders shall designate the directors to be elected by vote of the shares of new preferred stock and the Class B certificate holders shall designate the directors to be elected by vote of the shares of the new common stock. Certificate holders shall be permitted to vote by proxy.

(4) At the annual meetings of the stockholders of the corporation, the Voting Trustees shall vote the shares of new preferred stock for the election of such directors as shall have been designated by the holders of Class A certificates and shall vote the shares of new common stock for the election of such directors as shall have been designated by the holders of Class B certificates.

(5) Whenever, from time to time, the Company shall deliver Class A certificates to the Voting Trustees for cancellation, the Voting Trustees shall transfer to the Company such number of shares of new preferred stock as may be [fol. 77] equal to the number of shares represented by the Class A certificates surrendered for cancellation. Shares of the new preferred stock so delivered to the Company must be cancelled and retired forthwith by the Company.

(6) If any debentures or shares of new preferred stock are outstanding on April 1, 1946, the Voting Trustees shall, as holders of the legal title of all the outstanding shares of the Company, execute and file the consent in writing to a dissolution of the Company which is provided for under Section 39 of the Delaware Corporation Law, and shall take such other and further steps as may be necessary to dissolve and wind up the affairs of the Company in accordance with the laws of Delaware.

(7) If, as provided in the trust indenture, the Indenture Trustee shall declare the principal of all debentures due and payable because of a default, and shall notify the Voting Trustees in writing of such declaration of default, the Voting Trustees shall forthwith file the consent of dissolution under Section 39 of the Delaware Corporation Law

and take such other and further steps as may be necessary to dissolve and wind up the affairs of the Company in accordance with the laws of Delaware.

(8) If all debentures and shares of new preferred stock are retired on or before April 1, 1946, the Voting Trustees shall within a reasonable period of time after such retirement call a meeting of the holders of the Class B certificates to vote on the question of whether the Company should be dissolved. The presence in person or by proxy of the holders [fol. 78] of certificates representing a majority of the shares of new common stock then outstanding shall be required to constitute a quorum at such meeting. If the holders of certificates representing a majority of the shares represented at the meeting shall vote against dissolution, the Voting Trustees shall forthwith terminate the trust and distribute to the holder of each Class B voting trust certificate the number of shares of new common stock represented by such certificate; otherwise the Voting Trustees shall file the consent and take the other steps necessary to dissolve the Company, as provided in the preceding paragraph hereof. Any shares remaining with the Voting Trustees after distribution of the shares of common stock to the holders of Class B voting trust certificates shall be surrendered to the Company for cancellation and retirement. The Voting Trustees shall issue participating certificates representing fractions of shares, but the holders of such certificates shall be entitled to receive certificates for the new common stock of the Company only when assembled in full share amounts. The Company shall not be required to issue certificates for fractional shares of its new common stock.

(9) Each Voting Trustee shall receive not less than $250 or more than $500 per annum in full for all services rendered, the full amount of compensation to be fixed by the board of directors of the Company.

(10) Depositary, transfer, and other agents may be designated by the Voting Trustees, and such depositary, transfer, or other agents shall be entitled to reasonable compensation. The compensation of the Voting Trustees and of [fol. 79] their depositary, transfer and other agents, and all other expenses of the Voting Trustees and of the voting trust, shall be paid by the Company.

(11) The Voting Trustees, or either of them, may be removed at any time, with or without cause, and their successor or successors may be appointed, by the concurrent vote of the holders of a majority of the shares represented by the voting trust certificates of each class then outstanding.

XI. Reservation of Claims

All claims in favor of the Debtor or of the Debtor's estate not settled or adjusted in the reorganization proceedings, or in the plan, or in connection with the consummation of the plan, shall be retained and enforced by the Trustees. The Company shall cooperate with and assist the Trustees in every way in the prosecution and collection of such claims.

The Trustees shall have full power to prosecute pending actions and proceedings involving such claims, and to bring additional actions or proceedings in the courts of any jurisdiction. They shall also have full power to employ, retain, or displace, attorneys or counsel representing them in any action or proceeding, whether such action or proceeding be pending at the time of the consummation of the plan or not. They shall not, however, have any power to discontinue, compromise or settle any action or proceeding without the express approval of the Court.

The Court will retain continuing jurisdiction over such [fol. 80] claims and the prosecution thereof, and over the Company, its books, records and papers, and the Trustees, in connection therewith, after the final decree in the reorganization proceedings. The Court will from time to time fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of such claims, and the Company shall assume and pay the amount of such compensation as well as all other expenses incurred or paid by the Trustees in the prosecution, collection, or other disposition of the claims. If the value of the portfolio of the Company shall, at any time prior to a complete and final adjudication on the merits of all of the claims reserved to the Trustees, be $300,000 or less, the assets of the Company shall not be further depleted by purchases or redemptions of debentures or shares of preferred stock without order of the Court after a hearing upon notice to the Trustees. In such order the Court will

specify the financial arrangements to be made by the Company for the payment of all expenses then already incurred in connection with the claims as well as such other expenses as may reasonably be necessary in the further prosecution thereof.

The net proceeds ultimately resulting from the prosecution or other disposition of the claims will be paid to the Company.

XII. Miscellaneous Provisions

A. Prohibition of Non-Voting Stock

The certificate of incorporation of the Company shall provide that the Company shall be prohibited from issuing non-voting stock.

[fol. 81]

B. Reports of Company

Detailed reports of the Company, including profit and loss statements, balance sheets, and portfolio statements, shall be prepared in accordance with sound business and accounting practice, and copies thereof shall be mailed semi-annually to all holders of debentures and of Class A and Class B voting trust certificates.

C. Failure to Surrender Old Claims and Securities

Creditors, other than holders of debentures, who fail to file, assign, transfer, or release their claims, and holders of debentures or shares of old preferred and common stock who fail to present or surrender their securities, within such time as may be fixed in the final decree in the reorganization proceedings (which time shall not be sooner than five years after the final decree), shall lose all right to participate in the distribution under the plan, and the securities and other rights to which they would otherwise be entitled shall revert or pass to the Company.

D. Assumption of Tax Liabilities

The Company shall assume and agree to pay in full all tax liabilities owing by the Debtor or the Trustees to the United States of America or to any State. The claims of the United States shall have the same priority and preference over claims of other creditors of the reorganized

Debtor, with respect to the assets thereof, as would lie against the assets of the Debtor had the reorganization proceedings not intervened, and the United States of America shall be granted the same remedies against the reorganized [fol. 82] Debtor and its assets with regard to the collection of such liabilities as it had against the Debtor before reorganization. All statutes of limitation upon the collection of such claims shall be suspended during the pendency of the reorganization proceedings.

E. Form of Debentures and Voting Trust Certificates

The debentures and voting trust certificates to be issued to the holders of old debentures and old preferred and common stock shall clearly state the limitations upon and the nature of the future operations of the Company, and shall set forth the contingent nature of the future participation of the holders of the Class A and Class B voting trust certificates in the Company. The voting trust certificates shall be designated, respectively, as "Class A Liquidation Voting Trust Certificates" and "Class B Liquidation Voting Trust Certificates".

XIII. Approval, Acceptance, Confirmation and Consummation of the Plan

This plan shall be approved, accepted, confirmed and consummated in accordance with the provisions of Chapter X of the Bankruptcy Act, as amended. After confirmation, the plan shall be consummated by the Trustees acting under the supervision of the Court.

The Trustees shall have full power and authority to take any and all steps deemed by them to be necessary or proper to effectuate or to consummate the plan. Consistent with the terms of the plan and all applicable provisions of law, [fol. 83] they shall determine the terms, provisions and covenants to be omitted, added, changed or retained in the certificate of incorporation and the by-laws of the Company, the trust indenture, and all other instruments, documents or papers necessary or deemed by them desirable to consummate and carry out the plan or any provision thereof, and they shall determine the terms and provisions of the Voting Trust Agreement.

The Trustees may construe the plan, and their construction thereof or action thereunder shall be final and

conclusive. They may supply any defect or omission or reconcile any inconsistency in the terms of the plan in such manner or to such extent as may be necessary in their opinion.

The Company shall enter into any and all agreements and execute any and all documents which the Trustees or the Court may find necessary or proper in connection with carrying the plan into execution.

All costs and expenses of administration and all allowances which may be approved or made by the Judge, shall be paid in cash by the Trustees, or, after the consummation of the plan, by the Company.

The Company shall indemnify the Trustees, the Indenture Trustee, and the Voting Trustees against all loss, costs, liability and expense arising out of the administration of the reorganization proceedings, the plan, or any transaction required or authorized by the plan or by the Court in connection with the plan.

The Court shall retain jurisdiction over the assets dealt with in the plan, and over any and all persons, firms, or corporations to whom such assets may be transferred, and over all parties appearing in the reorganization proceedings for the purpose of carrying out and giving effect to [fol. 84] any and all provisions of the plan and the decree confirming the same.

EXHIBIT "B", ANNEXED TO ANSWER OF TRUSTEES

ORDER APPROVING PETITION IN REORGANIZATION
UNITED STATES DISTRICT COURT, District of New Jersey

In Proceedings for Reorganization

In the Matter of REYNOLDS INVESTING COMPANY, INC., a Corporation, Debtor

This matter being opened to the Court by Furst & Furst, Esquires, attorneys for petitioning creditors herein, upon the return of an order to show cause issued herein on the 18th day of May, 1938, hearings on which have been continued until this date, and it appearing that (1) the involuntary petition filed herein on May 18, 1938, by C. Suydam

Cutting, Clara B. Prince and Mary Van Pelt Bryan, three petitioning creditors having provable claims against the Debtor, and the amended involuntary petition of said petitioning creditors together with said order to show cause were duly served upon Debtor; (2) the Debtor, by Chadbourne, Hunt, Jaeckel & Brown and Merritt Lane, Esq., as [fol. 85] attorneys, filed an answer to said petitions and certain affidavits and exhibits; (3) James H. McIntosh, et al., certain preferred stockholders, and Everett L. Abernathy, et al., certain common stockholders, by Carter, Ledyard & Milburn, and Pitney, Hardin & Skinner, filed answers to the said involuntary petition, and Lum, Tamblyn & Fairlie and Blake and Voorhees having been duly substituted as attorneys for said James H. McIntosh, et al., preferred stockholders; (4) A Committee of Debenture Holders, represented by McCauley, Spiegelberg, Davis & Gallagher, and Frazer, Stoffer & Jacobs, having appeared; (5) A committee of Debenture Holders of which Dean Langmuir is Chairman, represented by Greenbaum, Wolff & Ernst, and a preferred Stockholders' Committee of which Alfred E. Dochez is Chairman, represented by Kellogg, Emery & Inness-Brown, and a Stockholders' Committee, represented by Percival E. Jackson, requested the Court to grant the relief prayed for by the petitioning creditors; (6) Albert E. Olson, Receiver of First Income Trading Company appearing by McCarter & English (George W. C. McCarter, Esq.) filed an answer to said involuntary petition; (7) Ralph E. Lum, of Lum, Tamblyn & Fairlie, having been present in open Court on behalf of certain preferred stockholders; (8) The Security Exchange Commission having appeared herein by Joseph L. Weinert, Edmund Burke, Jr., and J. Anthony Panuch, its attorneys; (9) a stipulation was entered into in open Court by all the parties who appeared herein, providing, among other things, that the answers heretofore filed to the said involuntary petition and amended involuntary petition be withdrawn, and that the Court approve of the petition and amended petition as herein filed in accordance [fol. 86] with Chapter 10 of the Bankruptcy Act of 1938 (Chandler Act); and no one appearing in opposition and no cause being shown to the contrary:

It is on this 19th day of January, 1939, on motion of Furst & Furst, attorneys aforesaid,

Ordered, adjudged and decreed:

1. That the applications for leave to withdraw each of the answers filed herein, be and the same are hereby granted.

2. That the petition and amended petition filed herein be, and they hereby are approved as duly and in good faith filed under Chapter 10 of the Bankruptcy Act of 1938, and as amended (Chandler Act).

3. That said petition and amended petition filed herein comply with the requirements of Chapter 10 of the Bankruptcy Act of 1938, and as amended (Chandler Act).

4. That by reason of the facts duly set forth in said petition and amended petition, relief under Chapter 10 of the Bankruptcy Act of 1938, and as amended (Chandler Act), is required, and that there is no adequate remedy except by the granting of such relief.

5. That it is necessary that Trustees be appointed for Debtor's estate.

6. That John Gerdes, No. 102 Maiden Lane, New York City, and James D. Carpenter, Jr., No. 75 Montgomery Street, Jersey City, New Jersey, be, and they are hereby [fol. 87] appointed Trustees of the Debtor's estate. The said Trustees, upon filing a bond, as hereinafter in this order provided, shall have all the title and shall exercise, subject to the control of this Court, and pursuant to the provisions of Chapter 10 of the Bankruptcy Act of 1938, and as amended (Chandler Act), all of the powers of a Trustee appointed pursuant to Section 44 of the said Bankruptcy Act and the same powers as those exercised by a receiver in equity to the extent consistent with Chapter 10 of the said Bankruptcy Act, and subject to the authorization and control of the Court, the power to operate the business of the Debtor until such time as the Court shall otherwise prescribe.

7. Without in any way limiting the generality of the powers and authority of the Trustees elsewhere in this order provided and to the extent consistent with Chapter 10 of the Bankruptcy Act of 1938, and as amended (Chandler Act), upon filing the bond provided for herein, the Trustees herein appointed be, and hereby are:

(a) Authorized and directed, pending further order of the Court in the premises, to take possession of and to run, manage, maintain, operate, keep in proper repair the assets, properties and business of the Debtor, real, personal or mixed, tangible or intangible, of whatsoever kind and description, and wheresoever situated, whether in this State, judicial district, and whether in the United States of America or elsewhere, and to manage, operate and conduct its business, and to this end to exercise its authority, franchises, and discharge all duties obligatory upon it, and [fol. 88] discharge and fix the compensation of all agents and employees, to collect and receive the income, rents, revenues, tolls, issues and profits of said assets, properties and business; to collect all outstanding accounts and all dividends and interest on securities belonging to it and to do all and every act necessary to carry on the business of the Debtor as an entirety, and exercise all and singular its rights, authorities, franchises and privileges in such manner, and to such extent as in the judgment of the Trustees may seem necessary or desirable;

(b) Authorized and empowered to prosecute, become party to, intervene in, compromise or defend suits and actions at law, or in equity, or otherwise in which the Debtor may have had or has any interest as plaintiffs, defendants or otherwise, and to be substituted as parties therein in an action heretofore commenced, pursuant to the order of this Court, and to proceed with said action in accordance with the terms of said order.

(c) Authorized and empowered to continue the operation of the business of the Debtor, as they shall determine, and to that end to employ and discharge and pay the compensation, salaries and wages of such officers, agents, employees and others heretofore accrued or to accrue as they deem necessary or advisable in connection with the custody, control, preservation, operation and management of the properties and business constituting the Debtor's estate, or [fol. 89] necessary or desirable to avoid detriment to the working organization of the business; to perform existing contracts, including leases of the Debtor, to the extent that performance thereof may seem to them desirable; to purchase and sell for cash, or on credit, any merchandise, or other property, real or personal, and to enter into and to

perform other contracts, in the regular course and conduct of the business of the Debtor, or otherwise; to let, sub-let, contract for the use of, turn to account or otherwise dispose of, buildings, public space, or other space owned, leased or operated by the Debtor, and any other property of any kind in relation thereto, or in connection therewith; to engage in any project deemed by the Trustees to be necessary, desirable or helpful in the promotion of the Debtor's business;

(d) Shall be and hereby are vested, without the doing of any further act, with full right, title and interest to all bank accounts, custody accounts, safe deposit boxes, if any, ownership of, or rights to which are now vested in the Debtor, and the respective depositaries shall forthwith transfer all such accounts and safe deposit boxes into the names of the Trustees as such appointed in this proceeding.

8. Within 5 days from and after the entry of this order, the said Trustees shall execute and file with the Clerk of this Court, a joint and several Surety Company bond to be approved by this Court, for the benefit of the United States, [fol. 90] in the sum of Fifty Thousand Dollars ($50,000.00), conditioned to the effect that the said Trustees will well and truly perform the duties of their office, and duly and faithfully account for all moneys and properties whatsoever that may come within their hands and abide by and perform all things which they shall be directed by this Court to perform.

9. The Trustees shall on or before the 10th day of February, 1939, give notice to creditors and stockholders of the Debtor, as same may appear upon the books of the Debtor by (a) mailing a copy to such creditors (including all known debenture holders, and their attorneys or attorneys-in-fact), stockholders at their respective addresses appearing on such books, and to the Commercial National Bank & Trust Company, Successor Indenture Trustee, and to the Securities and Exchange Commission; and (b) causing a publication to be made in the "Jersey Journal", a newspaper published and having a general circulation in the City of Jersey City, New Jersey, that a hearing will be held herein before this Court at the Federal Building, Newark, New Jersey, on Friday, the 17th day of March

1939, at ten-thirty o'clock in the forenoon of that day, or at such time or times to which any adjournment may be taken, for the purpose of hearing objections, if any, to the retention in office of the Trustees upon the ground that they are not qualified or are not disinterested, as provided in Section 158, Chapter 10, of the Bankruptcy Act of 1938 (Chandler Act).

10. That all of the expenses of administration as may [fol. 91] be fixed and determined by the Court in this proceeding, shall constitute a prior charge upon the Debtor's estate and shall be paid by the Trustees or their successor or successors, in accordance with the orders of the Court in this proceeding, without further order herein.

11. That all creditors, stockholders, and all persons claiming or acting by, through or under them, and all sheriffs, marshals and other like officers, agents, attorneys, solicitors, representatives, and employees, and all other persons, firms, associations and corporations, are hereby enjoined and restrained from instituting, continuing or prosecuting any action at law or suit or proceeding in equity or any other proceeding against the Debtor in any court of law or equity, or before any association, organization, or arbitration or Referee or umpire or other court or tribunal or otherwise, or from executing or issuing, or causing the execution or issuance, or the issuing out of any Court or any public office of any writ, process, summons, attachment, subpoena, replevin, execution or other proceeding, for the purpose of impounding or taking possession of, or interfering with the property constituting the Debtor's estate, or attempting to take into possession any part of the property constituting the Debtor's estate wheresoever located, whether in this state, judicial district, United States or elsewhere; and all other persons, firms, associations and corporations, are hereby enjoined and restrained from removing, transferring, disposing of, or attempting in any way to remove, transfer or dispose of, or in any way interfere with any property, assets or effects in the possession of the Debtor, or owned by the Debtor, [fol. 92] whether in the possession of the Trustees or otherwise, and from doing any act or thing whatsoever, to interfere with the possession and management by the Trustees of its assets, properties and business, real, person- or mixed, tangible or intangible, of whatsoever kind and de-

scription, and wheresoever situated, whether in this state, judicial district, the United States or elsewhere, or to interfere in any manner, directly or indirectly, with the possession, operation or management by the Trustees of the Debtor's estate, or to interfere in any way with the Trustees in the discharge of their duties, or to interfere in any way with the administration and disposition of the affairs and properties constituting its estate. All persons, firms, associations, corporations, their agents, attorneys, representatives and employees are hereby enjoined and stayed from commencing or continuing any judicial proceeding to enforce any lien upon the estate of the Debtor until further order of this Court, or until after the final decree.

12. The Trustees shall prepare and file with this Court within thirty days from the date hereof a list of all security holders, as provided for by Section 164 of Chapter 10.

13. The Trustees shall, within thirty days from the date hereof, prepare and file a plan with this Court, or a report of their reasons why a plan can not be effected.

14. The creditors and indenture trustees shall file proofs of claim and stockholders shall file proofs of interest with the Trustees within thirty days from the date hereof, after [fol. 93] which date no such claim or interest may participate in any plan, except on order for cause shown.

And it is further ordered, adjudged and decreed:

1. That all attorneys for creditors or stockholders shall file with the Court a statement, as required by Section 210 of Chapter 10 of the Bankruptcy Act of 1938 (Chandler Act); and that every person or committee representing more than twelve creditors or stockholders shall file a statement as required by Section 211 of said Bankruptcy Act, within thirty days from the date hereof.

Guy L. Fake, District Judge.

I hereby certify that the foregoing is a true copy of the original on file in my office.

Benjamin F. Havens, Clerk, per Charles E. Jaeckel, Deputy. (Seal.)

[fol. 94] EXHIBIT "C", ANNEXED TO ANSWER OF TRUSTEES

ORDER CONFIRMING PLAN OF REORGANIZATION

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

In Proceeding for Reorganization

In the Mafter of Reynolds Investing Company, Inc., a Corporation, Debtor

The plan of reorganization heretofore filed herein by the Trustees in the office of the clerk of this Court on March 29, 1940 having been approved by order of this Court dated April 19, 1940; and this Court having made an order, dated May 31, 1940, directing John Grimshaw, Jr., Esq., Special Master, to give notice to the debtor, the creditors and stockholders, the Indenture Trustee, the Securities and Exchange Commission, the Secretary of the Treasury, and such other parties and committees as have intervened or appeared in these proceedings, of a hearing to be held for the consideration of confirmation of said plan and of such objections as may be made to the confirmation; and the said plan having been considered, and due consideration having been given thereto, and the Court having been fully advised in the premises,

Now, upon reading the said plan of reorganization filed herein on March 29, 1940 by the Trustees, and the order herein approving the same, dated April 19, 1940; and it appearing from the affidavit of Evelyn Hamm, clerk in the [fol. 95] office of John Grimshaw, Jr., Esq., Special Master, sworn to June 12, 1940, that notice of said hearing for the consideration of the confirmation of said plan and of such objections as may be made to the confirmation was given to the debtor, the creditors and stockholders, the Indenture Trustee, the Securities and Exchange Commission, the Secretary of the Treasury, and such other parties and committees as may have intervened or appeared in these proceedings, as required by order of this Court dated May 31, 1940; and upon all the testimony, papers and proceedings heretofore had herein; and the Court being satisfied that (1) the provisions of article VII, section 199, and article X of Chapter X of the Bankruptcy Act have been complied with, (2) the plan is fair and equitable, and feasi-

ble, (3) the proposal of the plan and its acceptance are in good faith and have not been made or procured by means or promises forbidden by the Bankruptcy Act, (4) all payments made or promised by the debtor, or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge, and (5) the identity, qualifications, and affiliations of the persons who are to be directors or officers, or voting trustees, if any, upon the consummation of the plan, have been fully disclosed, and the appointment of such persons to such offices, or their continuance therein, [fol. 96] is equitable, compatible with the interests of the creditors and stockholders and consistent with public policy; and it further appearing that the said plan has been accepted in writing, filed in court by or on behalf of creditors holding two-thirds in amount of the claims filed by holders of debentures, and allowed, and by and on behalf of stockholders holding the majority of the shares of stock of which proofs have been filed and allowed of each class;

It is, on this 17 day of June, 1940, upon motion of John Gerdes and James D. Carpenter, Jr., as Trustees,

Ordered, adjudged and decreed

1. The said plan of reorganization is hereby in all respects confirmed.

2. The title to all of the debtor's property, real and personal, wherever situated, except claims belonging to the debtor or to the debtor's estate which have not been settled or adjusted in the reorganization proceeding, shall be transferred in accordance with the said plan to the debtor, and said property so transferred to the debtor shall be free and clear of all claims and interest of creditors and stockholders, except such claims and interests as may otherwise be provided for in the plan, or in this order, or in any other order directing or authorizing the transfer or retention of such property.

3. All claims in favor of the debtor or the debtor's estate not settled or adjusted in the reorganization proceeding

shall be retained and enforced by the Trustees, as provided [fol. 97] in the plan.

4. The debtor shall comply with the provisions of the said plan, the provisions of this order, and other orders of the Court relative to said plan.

5. All persons, firms or corporations are directed to perform and carry out all acts by each of them required to be performed or carried out pursuant to the provisions of this plan and the orders of the Court relevant thereto.

6. The Trustees shall transfer to the debtor all the assets of the debtor excepting the claims hereinbefore provided to be retained by the Trustees.

7. The Trustees, the Indenture Trustee, and all other parties or persons shall execute and deliver or join in the execution and delivery of whatever instruments may be necessary to effectuate the foregoing transfers of the property of the debtor and to effectuate all other provisions of said plan of reorganization.

8. The Trustees and all other necessary persons or parties shall do any and all acts which may be necessary, or found desirable by order of this Court upon recommendation of the Trustees, to effectuate the distribution to creditors, stockholders and others of the cash, securities or other property provided to be distributed to them under the terms of said plan of reorganization.

9. The costs and expenses of administration and such [fol. 98] other allowances as shall hereafter be approved by the Court, shall be paid.

10. All applications for allowances for services rendered herein shall be filed on or before July 17, 1940 with John Grimshaw, Jr., Esq., Special Master, and all applications which are so filed are hereby referred to said John Grimshaw, Jr., Esq., as Special Master, to conduct a hearing thereon, and to consider and report thereon. Such hearing shall be held in the Bankruptcy Courtroom, Post Office Building, Montgomery and Washington Streets, Jersey City, New Jersey, at 10 A. M. on the 20th day of August, 1940, and on subsequent dates to which the hearing may be adjourned.

11. The Special Master shall file his report containing findings and recommendations on the foregoing matters as soon as practicable in the office of the Clerk of this Court, and mail, not later than the following day, notice of the filing of such report to the Trustees, to all parties who have appeared or intervened in the proceedings, or their attorneys, and to such additional parties in interest as may file with the Special Master a written request for such notice.

12. Written exceptions, if any, to the report of the Special Master may be filed in the office of the Clerk of this Court by the Debtor, the Trustees, any creditor or stockholder, or any other party in interest, not later than ten days after the filing of such report. The person filing the exceptions shall mail or otherwise serve, not later than the day following the filing, copies of the exceptions upon the Special Master, the Trustees, and all parties who have appeared [fol. 99] or intervened in the proceedings or their attorneys.

13. A hearing upon the matters referred to the Special Master, the report of the Special Master, and all exceptions filed to such report, shall be held before this Court on the 7th day of October, 1940, and on any subsequent dates to which such hearing may be postponed or adjourned, at 10:30 A. M., at the United States Post Office Building and Court House, Federal Square, Newark, N. J., at which time creditors, stockholders and other parties in interest may be heard.

14. Any hearing may be continued, postponed or adjourned, from time to time, without notice other than announcement at the hearing or at the last previous postponed or adjourned hearing.

15. A written notice of the foregoing hearings, giving the times and places of such hearings, the names and addresses of all applicants for allowances, the amounts requested and such other information as may be appropriate, shall be mailed by the Special Master, on or before July 31st, 1940, to the debtor, the Trustees, the creditors and stockholders, the indenture trustee, the Secretary of the Treasury, the Securities and Exchange Commission, and such other parties and committees as may have intervened or appeared in these proceedings, at their last known addresses.

16. The debtor shall pay all the costs and expenses of administration as shall hereafter be approved by the Judge after hearing upon notice as provided in Sections 62(d) [fol. 100] and 247 of the Bankruptcy Act, and no other sums shall be paid by the debtor or by any other person, for services and for costs and expenses in the proceeding or in connection therewith, or in connection with the plan or incident to the reorganization.

17. The Trustees and the debtor shall report in writing to this Court within 30 days from the date hereof, and every 30 days thereafter, until the entry of a final decree, the acts taken and the progress made in the consummation of the plan.

18. The Trustees shall have full power and authority, as provided by the laws of the State of Delaware, to put into effect and carry out the plan and the decrees and orders of the Court relative thereto and may take any proceeding and do any act provided in the plan or directed by such decrees and orders, without the necessity of further action by the directors or stockholders of the debtor. Such power and authority may be exercised, and such proceedings and acts may be taken, as may be directed by such decrees or orders, by the Trustees with like effect as if exercised and taken by unanimous action of the directors and stockholders of the debtor.

19. Holders of debentures and of shares of preferred and common stock issued by the debtor prior to the initiation of these proceedings, shall on or before February 1, 1946, or five years after the final decree in this proceeding closing the estate, whichever of such dates is later, present and surrender their securities to secure the new securities provided [fol. 101] to be issued to them under the plan of reorganization, after which time no holder of debentures or shares of the preferred or common stock shall participate in the distribution under the plan.

20. The Court has considered the identity, qualifications and affiliations of Dean Langmuir, G. Vernon Rogers, Samuel S. Rodman, Richardson Morris and Edwin H. Woarms, who are to be directors of the debtor, and Arthur T. Vanderbilt and Charles F. Lynch, who are to be voting trustees under the voting trust for which provision is made in the

plan of reorganization, and the Court finds that their service as such directors and voting trustees is equitable, compatible with the interests of the creditors and stockholders, and consistent with public policy.

21. The order of the Court herein dated January 26, 1939, is hereby modified by the elimination of paragraphs "(9)", "(10)" and "(11)".

Guy L. Fake, District Judge.

I hereby certify that the foregoing is a true copy of the original on file in my office.

Benjamin F. Havens, Clerk, Per E. T. Pettengill, Deputy.

[fol. 102] IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

Affidavit of David Paine

STATE OF NEW YORK,
County of New York, ss:

David Paine, being duly sworn, deposes and says:

1. I am one of the attorneys for the petitioners. I am familiar with the proceedings had in the Actions referred to in this proceeding as Actions Nos. 1 and 2 and the Globe Action. I acted as trial counsel in Action No. 1.

2. I have read the Answer of John Gerdes and James D. Carpenter, Jr., as trustees for Reynolds Investing Company, Inc., debtor, verified January 4, 1942, to the petition herein, and although I regard it as unnecessary to reply to said Answer, I shall in order to advise the Court of petitioners' position with respect to the allegations of said Answer comment upon the numbered paragraphs thereof seriatim.

Paragraph 1—Petitioners admit the allegations contained in the first and second sentences of said paragraph.

Paragraph 4—Petitioners deny the allegation and refer the Court to Paragraphs 2 and 3 of the stipulation executed by petitioners and plaintiffs and "so ordered" by Judge Fake, a copy of which is annexed to the petition as Ex-

hibit D, which contemplated an application by petitioners to this Court to fix their liens, etc.

[fol. 103] Paragraph 5—Petitioners deny this paragraph, and state that there was no agreement by petitioners as to the fixing of their compensation. The paragraph is simply a conclusion of law.

Paragraph 6—Petitioners deny this paragraph and refer the Court to the fact that no agreement whatsoever is pointed out by plaintiffs to the effect that compensation should be made by the District Court of New Jersey.

Paragraph 7—The allegations in this paragraph are irrelevant. The fact that Greenbaum, Wolff & Ernst were attorneys for the Langmuir Debenture Holders Committee in the reorganization, and that as such they were paid $21,000 for their services and $1,305.79 for their disbursements is purely irrelevant. It had no more to do with the services rendered in this lawsuit than the fact that these plaintiffs as trustees of Reynolds Investing Company, Inc., were paid $87,500 in 1940 as an interim allowance for services alleged to have been rendered by them. In the application made by Greenbaum, Wolff & Ernst as attorneys for the Langmuir Committee there was a specific proviso that such application did not cover compensation for services rendered in the New York Actions.

Paragraph 8—The same comment applies to the amount paid to Kellogg, Emery & Inness-Brown as attorneys for the Dochez Stockholders Committee for their services as such. In the petition of the firm of Kellogg, Emery & Inness-Brown there was a similar proviso that the petition therein did include services rendered in the New York Actions.

[fol. 104] Paragraph 9—The petitioners deny the allegations of this paragraph.

Paragraphs 10, 11, 12, 15, 17—Petitioners admit these allegations.

Paragraph 16 is denied, except that petitioners admit that as respective attorneys for the Dochez and Langmuir Committees they consented to the order of the United States District Court for the District of New Jersey, dated June

17, 1940, a copy of which is annexed to the answer as Exhibit C.

Paragraph 18—Petitioners deny the allegations of this paragraph. The stipulation referred to above, marked "So ordered" by Judge Fake on July 10, 1941, provides in its second and third paragraphs that application shall be made to the Supreme Court of New York for the determination of petitioners' liens.

Paragraph 19—Petitioners assert that the allegations of this paragraph are irrelevant; they admit, however, that they have not applied to the United States District Court for the District of New Jersey for any allowance for services rendered in connection with the New York actions.

Paragraph 20—Petitioners admit this allegation, subject to the approval of the Court.

The following paragraphs are conclusions of law and for that reason require neither denial nor admission: 2, 3, 13, 14, and the third sentence of Paragraph 1.

David Paine.

(Sworn to January 15, 1942.)

[fol. 105] In Supreme Court of New York, New York County

Hearings Before Walter, J., on Value of Services

March 31, 1942.

Before Hon. Carroll G. Walters, Justice

Appearances:

Satterlee & Warfield, Esqs. and Greenbaum, Wolff & Ernst, Esqs., Attorneys for Petitioners, By: David Paine, Esq., of Counsel.

John Gerdes, Esq., appearing for himself and James D. Carpenter, Jr., as Trustees for Reynolds Investing Company, Inc.

The Court: All right, gentlemen.

Mr. Gerdes: May it please your Honor, I would like to note on the record that I appear here again today, specially,

at the request of the Honorable Guy L. Fake, United States District Judge for the District of New Jersey, and request your Honor to postpone all further hearings or other steps in this matter, until the determination by the Appellate Division of an application which is now pending before the Appellate Division in what is the nature of a writ of prohibition, to test the jurisdiction of this Court.

[fol. 106] I believe that your Honor probably is familiar with the step taken this morning. I telephoned just as soon as I could at ten o'clock this morning to your secretary, to advise of the fact that the writ was being applied for, and that I would request at the hearing this afternoon that all proceedings be postponed until the determination of the merits of the application for the writ.

Mr. Paine: If your Honor please, I want to call your attention in the first place that Judge Fake, when the application was before him by the Trustees here to compel us to turn over papers and so on to him, and when this question of jurisdiction first arose, he made it a condition with a stipulation which was entered into then, that this matter be referred to this Court, and we make application to this Court, to fix the fees. Now, Judge Fake has informed us that he wanted these fees fixed by the Supreme Court of New York County where the case was tried. That may not be doing your Honor much of a favor, but that is his view of that matter.

Now on this question of this remarkable notice of motion we got this morning, which is to be presented on the 17th day of April to the Appellate Division, we got a notice of motion served late this forenoon in which the respondents here, the Trustees, are asking the Appellate Division to stay this proceeding and to stay your Honor. The petition reveals, however, the fact that they went before the Court with an order to show cause containing a temporary stay, and the Court refused to give it. All that they have is a notice of motion which can come before the Appellate Division.

Now we are prepared, and we can do it very briefly I [fol. 107] think despite the importance of this matter and the great amount of work that has been expended on it—we are prepared to proceed, and I think the Appellate Division has indicated that they do not require or favor a delay of this matter or this hearing, pending the outcome of any

motion that may be made on April 17th. Therefore, we are prepared to go ahead.

The Court: Let me see the papers that were served on you.

Mr. Paine: Yes, sir.

Mr. Gerdes: Your Honor, we were supposed to serve a copy on you.

The Court: Yes.

Mr. Gerdes: And one of the things I would like to ask your Honor is as to the most convenient time when service can be made. I don't believe I am qualified to serve it upon your Honor, because it must be served as a summons in an action, and being one of the parties to the action I cannot serve it upon you. But I would like your indulgence, and perhaps some officer of the court here could make the service, and make an affidavit. We would be glad to pay the usual fee.

Mr. Paine: We will concede it was made.

The Court: I will accept service.

Mr. Gerdes: Well, we have to have, I suppose, either a notice of appearance or an affidavit of service. May I ask one of the officers here——

The Court: (To the Clerk.) Mr. Bachmann, you can serve me.

Mr. Bachmann: Your Honor, it is already on the record.

The Court: He wants you to serve me.

Mr. Bachman: (Handing paper to the Court.) You are duly served.

[fol. 108] Mr. Gerdes: So I can get an affidavit later as to service.

The Court: I note from Paragraph 21 of the Petition which has just been served upon me the following: "The Trustees sought to initiate this proceeding for the equivalent of the former writ of prohibition by an order to show cause of this Court (meaning the Appellate Division) returnable April 2, 1942, the earliest day on which the matter may be heard. They requested the stay of all proceedings in the special proceeding pending before Mr. Justice Walter. They were informed today that their application for the order to show cause has been denied."

As the Appellate Division has denied a stay of this very hearing, it seems to me that I should of course proceed.

Mr. Gerdes: May I say a word on that, your Honor, and also on another matter that Mr. Paine raised. I cannot say what was in the mind of Mr. Justice Martin. As we state in our petition, there is no concealment of the fact we apprised the Court and everybody of the fact we made the application, and it has been denied. It seems to me that the reason that it was denied was a reluctance on the part of one branch of the court to stay another branch of the court, and that the Presiding Justice probably thought it was more seemly for the application to be made directly to the judge in the matter so that he might act on his own initiative, rather than be compelled by order of another court to cease his activities in the proceeding.

The Court: But the fact is, all you have is the fact of the denial; isn't that so?

Mr. Gerdes: That is all, your Honor, and in making the [fol. 109] statement I do not purport to state the actual views of Mr. Justice Martin, because I do not know what they are. I did not see him personally. The message came through his secretary.

Now there is another matter which I should like to correct upon the record, and that is the statement of Mr. Paine that Judge Fake desires this Court to pass upon these fees. The fact is that he has repeatedly told me and the other Trustee, and the attorney for the reorganized debtor in this proceeding, that he believes he has jurisdiction, and that this Court has no jurisdiction. He has entered an order permitting the Trustees to take the action which is contemplated here.

The Court: No. I will proceed.

Mr. Gerdes: May it be noted upon the record, then, that the Trustees do not participate in the remainder of the proceedings.

The Court: You decline to participate?

Mr. Gerdes: Yes, your Honor. We appear here only specially for the purpose of contesting the jurisdiction of the Court, and we cannot, under the authority given us by the Federal Court, submit to the general jurisdiction of this Court by participating in the hearing which your Honor proposes to hold.

The Court: Now that position is utterly untenable. There is no semblance of foundation for any such view. You have made your objection to the jurisdiction of the Court;

it has been considered; it has been overruled. I have incorporated in the order overruling it a specific statement to the effect that you have an exception.

Now you may again state on the record that you again [fol. 110] except to my ruling overruling the objection to jurisdiction. You have been overruled in that. It is your duty to proceed, and I will hold you in exactly the same position as if you had proceeded. I think there is no right in any litigant to come into a court and question the jurisdiction of the court, and then say, when it is overruled, "I decline to participate further", unless you are deliberately and intentionally intending that this matter of the fixation of the fees shall be fixed solely upon the evidence adduced by the petitioners.

Mr. Gerdes: May it please your Honor, I am here as the representative of the Federal Court.

The Court: You are here as a Trustee in Bankruptcy who has brought actions in this court, Mr. Gerdes.

Mr. Gerdes: As an officer of the Federal Court; and as such officer, I must abide by the wishes of the Court. My instructions have been not to participate in any hearing on the merits but to present the jurisdictional question, and to cooperate in every possible way with this Court and the other litigants to have a review of the question of jurisdiction by the higher courts, both state and federal.

The Court: There is nothing in my proceeding that is going to prevent or embarrass your reviewing the question of jurisdiction up to the Supreme Court of the United States.

Mr. Gerdes: Your Honor, I regret that I must retire.

(Exit.)

Mr. Paine: Your Honor, what I proposed to do, subject to your approval, is to then conduct an inquiry something in the nature of an inquest.

[fol. 111] The Court: Well, I don't want to characterize it. The facts speak for themselves, that the objections of the respondents to jurisdiction have been overruled. They were perfectly at liberty to take an objection again upon this hearing. I shall treat the record as if they have done so, and it has been again overruled, and they again have an exception to the overruling.

Mr. Paine: There is one stipulation, just to keep the record straight, that I would like to read. When this matter

came before Judge Fake on July 10, 1941 in his court in Jersey City—that is the motion to compel us to turn over papers to the Trustee which we claimed under our possessory lien—he allowed the motion to be withdrawn by the Trustees, although he indicated at the time that he believed he would deny it. He allowed it to be withdrawn on a stipulation which read in part as follows——

The Court: Well, that stipulation is one that is already a part of the record, isn't it?

Mr. Paine: Yes, sir. I just want to read a part of it, if I can find it.

The Court: Well, we are not going to go over the question of jurisdiction here again.

Mr. Paine: No, sir. Paragraph Three: "Upon conclusion of the reference before Philip Dunn, Esquire, in Gerdes vs. Reynolds, et al., and the entry of judgment thereon (at which time the relationship of attorney and client between petitioners and respondents shall terminate), respondents will commence proceedings for the fixation of their lien in accordance with the laws of the State of New York", and that is a part of the stipulation which was signed by both parties, and was marked "So Ordered" by the Judge.

Now, Mr. Warfield, will you take the stand?

[fol. 112] Ethelbert Warfield, residing at 400 East 52nd Street, New York City, called as a witness on behalf of the petitioners, having first been duly sworn, testified as follows:

Direct examination.

By Mr. Paine:

Q. Mr. Warfield, you are a member of the Bar of the State of New York?

A. I am.

Q. A member of the firm of Satterlee & Warfield at the present time?

A. Yes, sir.

Q. And were you formerly a member of the firm of Kellogg, Emery and Inness-Brown?

A. I was.

Q. Was that firm attorneys in three actions in the Supreme Court of New York County for the plaintiffs?

A. It was.

Q. In which Messrs. Gerdes and Carpenter were the plaintiffs, and they were Trustees, is that right?

A. It was.

Q. Now, state whether or not you had charge for the firm of Kellogg, Emery & Inness-Brown of those three suits?

A. I did, from the date on which the firm was first called into the matter.

Q. And when was that?

A. That was June 22, 1938. We were representing the corporation, not these particular plaintiffs, Gerdes and Carpenter, because they had not then been appointed Trustees.

Q. Yes. Now, what corporation was it you were representing?

A. Reynolds Investing Company, Inc.

Q. And in the three suits which I just mentioned, who were the defendants?

A. The defendants were C. K. Reynolds and a large group that I couldn't possibly name now, of about thirty-five defendants, I would say.

Q. Yes. That was in action No. One, we will say.

A. That is right.

[fol. 113] Q. And the same in action No. Two?

A. No. In action No. Two I think there were just C. K. Reynolds and William F. Woodward, and R. S. Reynolds, and R. S. Reynolds, Jr. R. S. Reynolds, Jr. was never served.

Q. And the third action, who was the defendant there?

A. I think it was the Globe Indemnity Company or Globe, some similar name.

Q. And in each of these three actions, were Messrs. Gerdes and Carpenter, acting as Trustees of the Reynolds Investing Company, plaintiffs?

A. Yes, although in the first action the company was a plaintiff first, and Gerdes and Carpenter were substituted.

Q. Yes. Do you recall when the first action was begun?

A. About August 4, 1938, we obtained an order; I think it was dated August 4th, and the company was served about that time.

Q. Now, was that company in the Federal Court at that time in any proceeding?

A. It was. There were proceedings pending under the old 77b, although there had not been at that time any adjudication.

Q. And at that time were Messrs. Carpenter and Gerdes—had they been appointed Trustees?

A. No, sir. They were appointed Trustees I believe on January 19, 1939.

Q. The year following that in which the action was begun?

A. That is right.

Q. Now the second action was begun in 1940, wasn't it? Do you recall?

A. I don't recall, but it was after the appointment of the Trustees.

Q. And the third action, you remember when that was begun?

A. That was quite long; that was probably 1940.

Q. Now I wish you could confine yourself to Action No. One and tell the Court briefly what was done in the way of [fol. 114] legal services in that action, beginning from the time that the action began on June 22, 1938, I think, down to November 6, 1941, which I think the record shows was the date judgment was finally entered in that action.

A. Not January 6, 1941.

Q. November 6, 1941. Did I say January?

A. Well, that is a considerable job.

The Court: Mr. Paine, when you and Mr. Gerdes saw me in chambers some time this month, I don't remember the exact date, I told you both that on this hearing I would follow the procedure of taking the schedule of services annexed to your petition as the direct examination, and permit him to simply cross-examine.

Mr. Paine: Well, I will follow that procedure. I didn't know but what he having withdrawn, that I would have to go into the thing more fully.

The Witness: Well, perhaps, your Honor, I could state I executed this petition, and that it states in reasonable detail the services rendered by my firm and our associate firm, the firm of Greenbaum, Wolff & Ernst, in connection with these proceedings, as an all-inclusive statement.

Q. Does it set forth also the number of hours that were necessarily devoted to the preparation and trial of the suit, and other incidentals in connection therewith?

A. It does.

Q. And you are acquainted in your supervision of the case with what was done, not only by Kellogg, Emery & Inness-Brown, but also by Greenbaum, Wolff & Ernst?

A. Yes. I was in almost daily conference with some [fol. 115] member of the firm of Greenbaum, Wolff & Ernst on this matter.

Q. And were the services as set forth therein necessary in conjunction with the prosecution of this action and the obtaining of the judgment?

A. I considered that they were in every detail.

Mr. Paine: I offer the petition in evidence with the schedules annexed to it.

The Court: It will be deemed marked in evidence.

(Petition received in evidence and deemed marked, Petitioners' Exhibit 1.)

The Court: It is already part of the file papers.

Mr. Paine: That seems to be all.

The Court: You are going to ask him the reasonable value of the services, aren't you?

Mr. Paine: All right.

Q. Mr. Warfield, are you acquainted with, or have you an opinion as to the reasonable value of the services which are contained in the petition and the other exhibits annexed thereto, which have been offered in evidence, and which is Petitioners' Exhibit 1?

A. I have.

Q. And basing your answer on the petition which you have testified to, what would you say was the fair and reasonable value of the services of the two firms, Kellogg, Emery & Inness-Brown, and Greenbaum, Wolff & Ernst, in the proceeding Number 1, Number 2 and Number 3—in those three actions?

[fol. 116] The Court: You will have to separate it.

Q. Well then, will you take Action No. 1 and state what in your opinion the reasonable value was in that action of the services of the attorneys for the plaintiff?

A. I would say in my opinion the reasonable value of the services in Action No. 1 is $145,000.

Q. And in Number 2?

A. I would say it was $5,000.

Q. And in Number 3?

A. I would say it was $100 Oh, I beg your pardon—$1,000.

Q. That would make $151,000 all told?

A. Yes, sir.

The Court: The Trustees may now cross-examine. (There was no response.)

The Court: Have the petitioners anything further?

Mr. Paine: I suppose, your Honor, that the judgments are considered to be in evidence. If not, I will offer the judgments which were entered here, in the Suit No. 1, in evidence.

The Court: All right. They will be deemed marked. They are already a record in this court.

(Judgments received in evidence and deemed marked, Petitioners' Exhibit 2.)

Mr. Paine: I think I will also offer in evidence, so that they be deemed offered in evidence, the files in the office of the County Clerk of New York County—the files in regard to this case. There are of course the report of the Referee [fol. 117] and various other matters which I think should all be deemed marked in evidence.

The Court: All right. They will be deemed marked.

(County Clerk's Files received in evidence and deemed marked, Petitioners' Exhibit 3.)

Mr. Paine: Mr. Greenbaum is here, and if your Honor wishes any cumulative evidence on this thing, I should be glad to supply it.

The Court: Well, I suppose Mr. Greenbaum agrees with Mr. Warfield; does he?

Mr. Paine: I think he does.

Mr. Greenbaum: In toto.

The Court: And Mr. Greenbaum is here for cross-examination by the Trustees if they so elect.

Mr. Paine: Yes, sir.

By the Court:

Q. In fixing the value, Mr. Warfield, I suppose of course you have taken into consideration the time consumed?

A. Yes, sir.

Q. And the nature of the work?

A. Yes, sir.

Q. Have you taken into consideration the results obtained?

A. I have, sir, to the extent of fixing a higher value on services in Action Number 1 in which judgments have been obtained, although up to the present time collections have not been made on those judgments.

Q. Have you taken into consideration the extent to which the judgments are collectible, or rather, the judgment. [fol. 118] There are two separate judgments in action No. 1, are there not?

A. Yes, sir.

Q. Have you taken into consideration the extent to which those judgments are collectible?

A. Yes, sir; but I have no final information on the amount to which they are collectible, and whether or not the testimony of the services rendered in the first action will result in the collection of the judgments eventually.

Q. You say you have taken into consideration the extent to which the judgments are collectible. What have you figured as the extent to which they are collectible?

A. Well, we have information from the Trustees that the judgments collectible against C. K. Reynolds and the people against whom the judgments have been obtained, will be divided one-half between this judgment, and one-half the judgment of the Continental Securities Corporation. The only figures I have heard from these gentlemen is that the total that will be collectible will be between $300,000 and $400,000 from the Reynolds group. But that does not include the moneys collected or collectible from other defendants, such as Prentice and Brady, who have so far paid $18,000, and other minor amounts, which should total another $15,000.

Q. Do you mean that the $300,000 to $400,000 is what these Trustees will get from the Reynolds group, or do you mean that is the total collectible, to be divided between these Trustees and the Continental Trustees?

A. That is the total that will be collected and divisible between the two. But, if your Honor please, they still have an action in Virginia——

Q. Wait just a moment. And on that state the reasonable [fol. 119] value of your services is just about equal to what will be collected, isn't it?

A. If they are correct and that is all that is collectible, it is; yes, sir.

Q. Now, have you regarded the services in this action, that is this Action No. 1, as being of any benefit to the Trustees in other actions, in other courts?

A. Well——

Q. I have specifically in mind the action against R. S. Reynolds in Virginia.

A. We have specifically excluded from this application compensation for any services actually rendered in that action. But we have considered that the services rendered here are of the first importance in the action in Virginia.

Q. You have attributed to the services rendered in Action Number 1 some element of benefit to the Trustees as a result of their actions against R. S. Reynolds in Virginia?

A. Yes, sir. I might say that the petition shows, your Honor, that a stipulation was entered into in which our services were used, under which the testimony taken in the New York action may be introduced as binding upon the parties in the Virginia action.

Q. You say such a stipulation has been entered into?

A. Yes, sir.

Q. That the testimony taken here upon the trial of Action No. 1 may be used in the trial of the action in Virginia?

A. That is right, sir. It appears in this petition.

Q. I see. All right, that is all I have.

By Mr. Paine:

Q. You spoke of the "Reynolds group", Mr. Warfield. Will you tell us what you meant by that?

A. Well, of course I mean the Reynolds group; the [fol. 120] two Reynolds groups, really; C. K. Reynolds and Woodward here in New York, and R. S. Reynolds and R. S. Reynolds, Jr. in Virginia. By the Reynolds group in this action I mean C. K. Reynolds and C. K. Reynolds, Jr.

Q. Now, in coming to your——

The Court: C. K. Reynolds, Junior? Is there any C. K., Junior?

The Witness: Yes, sir. He was a partner in Granberry & Company, your Honor.

Q. Did you, in fixing the amount of fee, take into consideration at all whether or not R. S. Reynolds, the Virginia defendant who was not served in this suit—whether

or not he was able to pay such judgment as might be obtained against him in that suit?

A. I did.

Q. And what consideration did you give that, and what conclusion did you come to?

A. Well, in connection with several conversations which were carried on partly by our two firms, it was developed that Mr. R. S. Reynolds was financially able to pay a considerable judgment; and also it is a matter of public record that he is receiving compensation at the rate of $100,000 a year from the company of which he is president, the Reynolds Metal.

By the Court:

Q. Now let me see if I understand you. Do you say your information from the Trustees is that from 3 to 4 hundred thousand dollars is the amount collectible from C. K. Reynolds and Woodward, and R. S. Reynolds?

A. No. C. K. Reynolds only, sir. I have heard different figures mentioned—350, 375, and just over $400,000.

[fol. 121] Q. But that excludes R. S. Reynolds entirely?

A. Yes, sir. And I know, if your Honor please, that at one time Mr. R. S. Reynolds said that he was prepared to go on record as stating that his total assets that he could use in the settlement of any lawsuit would not exceed $600,000.

By Mr. Paine:

Q. Do you know whether or not that case in Virginia was adjourned by the Trustees, or not?

A. I understand it has been from time to time, and it is now adjourned to some time, as I recall, about June.

Q. Yes, of this year?

A. That's right.

Colloquy Between Court and Counsel.

Mr. Paine: I think that is all, Mr. Warfield.

The Court: Well now, just this one thought occurs to me. You are having this proceeding before me, and I presided at the trial of the action.

Mr. Paine: Yes, sir.

The Court: Of course I am going to think about what I learned at that trial.

Mr. Paine: Yes, sir.

The Court: Do you want me to consider or disregard the evidence taken upon that trial?

Mr. Paine: Well, I think that should be certainly considered, and I ask your Honor to do it.

The Court: Well, it was all taken down stenographically and was printed as we went along.

Mr. Paine: Yes, sir.

The Court: And in the case of any appeal, there would be no substantial expense in submitting that record to the [fol. 122] Appellate Division, or any other court; would there?

Mr. Paine: That is correct, and I offer that record in evidence.

The Court: That will be deemed marked in evidence.

(Received in evidence and deemed marked, Petitioners' Exhibit 4.)

Mr. Paine: There is one other matter I think I should call your attention to. The Courts of this state have held, of course, that the minute the services are terminated by the discharge of the attorneys, then they have a cause of action from that time; regardless of what may thereafter eventuate, the statute of limitations runs from that moment. It has been so held in the case of *Adams* v. *the Fort Plain Bank;* and also in that same case——

The Court: Why don't you give the citation?

Mr. Paine: Yes, sir; 36 N. Y. 255; *Adams* v. *The Fort Plain Bank*. It was also said by Chief Judge Davies in that case that interest runs from the day on which the services terminated; that is the day on which the demand came due, and I shall ask your Honor to allow us interest at six per cent on this, on the following basis. It will have to be proportioned, I should think, because the letter of discharge which we got was June 3, 1941. But that of course did not terminate the matter, because we went ahead and were asked to go ahead with the reference before Mr.

[fol. 123] Dunn. The whole matter terminated on November 6, 1941, and therefore it seems to me that there will have to be an allocation or proportionate amount of interest to the principal divided in that way.

I suggest, for the purpose of the record, that I simply put Mr. Greenbaum on the stand just to confirm what Mr. Warfield said.

The Court: All right.

Mr. Paine: There is one other case, your Honor, which I think I should call to your attention. That is the case of *Martucci* v. *Brooklyn Children's Aid Society*. That is in 284 N. Y. 408. It is a case somewhat along the lines of the *Tillman* case except that it refers to the fact that the amount of recovery of the settlement will depend on factors, with some of which the respondent, who was actually the attorney there, would have no concern, because he had been discharged.

The Court: I don't get the drift of that.

Mr. Paine: Well, the idea is this: subsequent events in regard to settlement of the action after the attorney has been discharged, and what was realized, and so on, were held in that case not to be the basis on which any award or any fee could be fixed for him.

The Court: Well, by calling it a subsequent event, you can't prevent there being taken into consideration the amount of benefit, can you?

Mr. Paine: Well, I suppose the benefit——

[fol. 124] The Court: In other words, the extent to which services are beneficial is one of the elements to be considered, isn't it?

Mr. Paine: Yes, I think so. Of course in this case I take it that the results obtained, which is the term usually used by the courts—the results obtained were judgments aggregating over a million dollars. That was when our services ended. Now, how successful these gentlemen will be in collecting that sum under the methods which they have applied, I think had very little to do with it.

Lawrence S. Greenbaum, residing at 724 Stuart Avenue, Mamaroneck, New York, called as a witness on behalf of

the petitioners, having first been duly sworn, testified as follows:

Direct examination.

By Mr. Paine:

Q. Mr. Greenbaum, you are a member of the Bar of the State of New York?

A. I am.

Q. And were you a member of the firm of Greenbaum, Wolff & Ernst during the time in which the services were rendered in this action, as set forth in the petition which has been filed here, Exhibit 1?

A. I was.

Q. And are you acquainted with the petition?

A. I am.

Q. Does it correctly set forth the number of hours that were necessarily devoted to the preparation and trial of the action, and obtaining the judgment?

A. It does.

Q. And does it also set forth correctly the services that were rendered in connection with the three actions which [fol. 125] are mentioned in it?

A. It does.

Q. Now, you heard Mr. Warfield's testimony in this proceeding just given, have you?

A. I have.

Q. And if the specific questions which were asked him, both by his Honor and by me, were asked you, will you state whether or not your testimony would be the same as his?

A. It would.

Q. In all respects?

A. Except I would like to limit the expert testimony that Mr. Warfield gave on the value of the services.

Q. Well, will you state what in your opinion was the value of the services?

A. In coming to the same conclusion that Mr. Warfield has, I feel that where attorneys are discharged, I measure the value of the services from the hours point of view of the attorney as well, and I feel that the figures that he arrived at would be substantiated without taking into consideration the question of any recovery.

Q. Yes.

A. As a cost to us.

The Court: Has any payment been received on account?
The Witness: None.
Mr. Paine. No sir.
The Court: All right.
Mr. Paine: The petitioners rest.
The Court: All right. Now, despite the fact that the respondent Trustees have not participated in the hearing and have absented themselves from the court room, I am going to adjourn the further hearing of this matter to Monday, April 6th, at 10 A. M. in the New York County Court House, in the Trial Term to which I am assigned to sit next [fol. 126] month, Trial Term Part VII. And I will request counsel for the petitioners to advise the Trustees not later than tomorrow that I have so adjourned the further hearing, for the express purpose of giving them an opportunity to come in and present anything further that they desire—or present anything that they desire; and particularly to advise them that I would appreciate hearing from the Trustees their opinion as to the value of the services.
Mr. Paine: Would it be possible, your Honor, to make that a day or two later in that week? I am going to be away on the sixth.
The Court: What date do you prefer?
Mr. Paine: Well, I should prefer Thursday or Friday of that week.
The Court: All right. Thursday the 9th, then, instead of April the sixth.
Mr. Paine: We will advise Mr. Gerdes what your Honor says:
The Court: All right.

(Further hearing adjourned to Thursday, April 9, 1942 in the Court Room of Trial Term Part VII, New York County, 10 A. M.)

[fol. 127] (Adjourned from March 31, 1942.)

Room 335, County Court Building,
New York, N. Y., April 8, 1942.

Before Honorable Carroll G. Walter, Justice.

APPEARANCES:

Satterlee & Warfield, Esqrs. and Greenbaum, Wolff & Ernst, Esqrs., Attorneys for Petitioners, by David Paine, Esq., of Counsel.

The Court: Mr. Paine, did you notify the respondents that at the last hearing I announced I would hear any evidence which they desired to present?

Mr. Paine: Yes, sir. If Mr. Dwyer will take the stand, I will prove that.

James F. Dwyer, 53 Wellington Court, Brooklyn, N. Y., called as a witness on behalf of the petitioners, being duly sworn, testified as follows:

Direct examination.

By Mr. Paine:

Q. Mr. Dwyer, are you an attorney-at-law of the State of New York?

A. Yes, sir.

[fol. 128] Q. Associated with the firm of Satterlee & Canfield, attorneys for the petitioners in this proceeding?

A. Satterlee & Warfield.

Q. Did you cause to be sent any letters to Mr. John Gerdes, respondent in this case?

A. Yes, sir, and also to James D. Carpenter, Jr., one of the respondents.

Q. And how about Colonel Twombly?

A. A letter also was sent to Colonel Twombly.

Q. From the offices of Satterlee & Warfield, is that right?

A. Yes, sir.

Q. And have you copies of those letters there?

A. Yes, sir.

Q. And were those letters sent on the dates which they bear?

A. The letter to Messrs. Gerdes & Carpenter was sent on March 31, 1942.

Mr. Paine: I offer that in evidence.

(Received in evidence and marked Petitioners' Exhibit 5.)

Q. Was there a second letter sent to these same respondents, Gerdes & Carpenter?

A. I understand there was, and I have a copy of it before me.

Q. And do the files of Satterlee & Warfield show that such a letter was sent?

A. Yes, they show that a letter was sent at 4:40 P. M. on April 1st.

Mr. Paine: I offer that in evidence.

(Received in evidence and marked Petitioners' Exhibit 6.)

The Witness: I may say, Mr. Paine, that copies of Ex-
[fol. 129] hibits 5 and 6 were sent to Mr. Twombly on April 1st at 4:40 P. M.

Q. Duplicate copies?
A. Yes, sir.

The Court: Who is Mr. Twombly in this case?
The Witness: Mr. Twombly is a member of the firm of Twombly, Putney & Hall, counsel for the Reynolds Realization Corporation.

Q. Did the Reynolds Realization Corporation, under the reorganization, succeed to the rights of the Reynolds Investment Company?
A. Yes, sir.
Q. And Mr. Twombly or his firm have not appeared in this particular proceeding, have they?
A. No, sir.
Q. But was his firm counsel in the reorganization proceedings?
A. For the reorganized company, yes, sir.
Q. Now, have you a third letter?
A. This is the letter sent to Colonel Twombly in which was enclosed copies of Exhibits 5 and 6.

Mr. Paine: I offer that letter in evidence.

(Received in evidence and marked Petitioners' Exhibit 7.)

Mr. Paine: We, your Honor, have also received, or Mr. Greenbaum has, a copy of a letter addressed to your Honor by Mr. Gerdes, and I think that I will offer that letter in evidence, to keep the record straight.

[fol. 130] The Court: Yes, I received that letter this morning.
Mr. Paine: I offer it in evidence.

(Received in evidence and marked Petitioners' Exhibit 8.)

Q. Mr. Dwyer, I show you paper marked, "Annual Report, Reynolds Realization Corporation as of December 31, 1941," and ask you whether or not that is the report which was issued by the Reynolds Realization Corporation bearing the certificate of Barrow, Wade, Guthrie & Co.?

A. Yes, sir.

Mr. Paine: I offer in evidence, if your Honor please, so much of that report as recites as follows: "During the year 1941 the Corporation received an aggregate of $34,522.37 from the liquidators of the firm of Prentice & Brady, under the judgment of the New York litigation described as 'Action Number 1', in Note 3 of the Balance Sheet."

I think that is all, Mr. Dwyer.

(Witness excused.)

The Court: The crier will please call John Gerdes and James D. Carpenter as Trustees in Bankruptcy of Reynolds Investing Company.

(The Court Officer reported that there was no answer.)

Mr. Paine: If your Honor please, at the last hearing in The Bronx, I called your attention to the fact that although we were discharged by the letter of June 5, 1941 from all [fol. 131] except attendance at the reference before Mr. Dunn, that after that date and until November 2nd, I think I put it—it was really November 27th—1941, we were engaged in the limited services of conducting the reference before Mr. Dunn and entering judgment thereon, and I would like to put Mr. Greenbaum on the stand just to show the number of hours of the total which we devoted to that reference.

The Court: That is included, is it not, in your affidavit attached to your petition?

Mr. Paine: Yes, sir. The only purpose of it is on the matter of interest from those two dates.

The Court: All right. You may put him on. I shan't go back of the November date.

Lawrence S. Greenbaum, recalled as a witness in behalf of the petitioners, having been previously sworn, testified further as follows:

Direct examination.

By Mr. Paine:

Q. Mr. Greenbaum, did you have charge for the respondents here of the reference held before Mr. Dunn in Action Number 1?

A. I did.

Q. In the period after the letter of discharge here, which was a part of the petition which was offered in evidence, June 3, 1941, did you continue the services as outlined in that letter before the referee?

A. We all did, and I think the date is June 5th, Mr. Paine.

[fol. 132] Q. June 5th?

A. Yes.

Q. I think that is the date when we started and that the letter itself which discharged us in the rest of the proceeding from any services therein was on the 3rd, isn't that correct?

A. (No answer.)

Q. Can you state how many hours of the total as has already been testified to were devoted to that reference after June 3, 1941?

A. After that date there were devoted 437¾ hours, as against a total of 8814½ hours.

Q. And of that 400-odd hours, how much was partners' time and how much was associates' time?

A. There were 76¾ hours of partners' time and 361 of associates' time.

Mr. Paine: I think that is all.

(Witness excused.)

The Court: The stipulation of July 9, 1941, Mr. Paine, provides that upon conclusion of the reference before Philip Dunn, Esq., in Gerdes against Inness and the entry of judgment thereon the relationship of attorney and client between petitioners and respondents shall terminate.

I don't think I can go back of the entry of judgment and that date I understand is November——

Mr. Paine: November 27, 1941.

The Court: November 27th.

(The Court thereupon rendered his decision as follows:)

[This decision is printed herein as the Opinion of Walter, J., on Order Fixing Lien and Amount of Attorneys' Compensation, at pages 162-168.]

[fol. 133] NOTE RE PETITIONERS' EXHIBIT 1

This exhibit is identical with the Petition of B. H. Inness Brown, et al.

(Printed herein at pages 18 to 42.)

NOTE RE PETITIONERS' EXHIBIT 2.

Judgments entered in Suit No. 1.

(Omitted pursuant to stipulation.)

NOTE RE PETITIONERS' EXHIBIT 3.

Files from office of County Clerk of New York County in regard to this case.

(Omitted pursuant to stipulation.)

NOTE RE PETITIONERS' EXHIBIT 4.

Stenographer's minutes of trial in case of Gerdes, et al. v. Reynolds, et al.

(Omitted pursuant to stipulation.)

[fol. 134] PETITIONERS' EXHIBIT 5.

Satterlee & Warfield, 49 Wall Street, New York

March 31, 1942.

John Gerdes, Esq., 1 Wall Street, New York, New York.

James D. Carpenter, Jr., Esq., 75 Montgomery Street, Jersey City, New Jersey.

Re: In the Matter of the Petition of B. H. INNESS BROWN, et al.

GENTLEMEN:

At the conclusion of the hearing before Justice Walter this afternoon, Mr. Justice Walter directed us to advise you that he was adjourning the hearing for the express purpose of giving you an opportunity to come in and present anything that you desired and particularly that he would appreciate hearing your opinion as to the value of services rendered by the firms of Kellogg, Emery & Inness-Brown and Greenbaum, Wolff & Ernst.

An exact transcript of Mr. Justice Walter's remarks is as follows:

"The Court: Now, despite the fact that the Respondent-Trustees have not participated in the hearing and have absented themselves from the court room, I am going to adjourn the further hearing of this matter to Monday, [fol. 135] April 6th, at 10 A. M. in the New York County Court House in the trial term to which I am assigned to sit next month, Trial Term Part 7, and I will request counsel for the Petitioners to advise the Trustees not later than tomorrow that I have so adjourned the further hearing, for the express purpose of giving them an opportunity to come in and present anything further that they desire, or present anything that they desire; and particularly to advise them that I would appreciate hearing from the Trustees their opinion as to the value of the services."

Upon application of counsel, Mr. Justice Walter adjourned the hearing for the purposes indicated above, to

10 A. M. April 9th, at Trial Term, Part VII of the Supreme Court, New York County.

Very truly yours, Satterlee & Warfield and Greenbaum, Wolff & Ernst.

JFD:des

[fol. 136] PETITIONERS' EXHIBIT 6.

Satterlee & Warfield, 49 Wall Street, New York

April 1, 1942.

John Gerdes, Esq., 1 Wall Street, New York City.

James D. Carpenter, Jr., Esq., 75 Montgomery Street, Jersey City, New Jersey.

DEAR SIRS:

Re: In the Matter of the Petition of B. H. INNESS BROWN, et al.

Referring to our letter of March 31st, Mr. Justice Walter, on our application, has adjourned the hearing for the purposes indicated in his remarks quoted in our letter of March 31st, to 10 A. M. April 8th at Trial Term, Part VII of the Supreme Court, New York County, instead of the same hour on April 9th.

Very truly yours, Satterlee & Warfield, Greenbaum, Wolff & Ernst.

EW/MB

[fol. 137] PETITIONERS' EXHIBIT 7.

Satterlee & Warfield, 49 Wall Street, New York

April 1, 1942.

Edward B. Twombly, Esq., Putney, Twombly & Hall, 165 Broadway, New York City.

DEAR COLONEL TWOMBLY:

Re: In the Matter of the Petition of B. H. INNESS BROWN, et al.

I am enclosing, for your information, a copy of a letter which we sent yesterday to Mr. Gerdes and Mr. Carpenter

at the request of Mr. Justice Walter, and a copy of a letter which we are sending to Mr. Gerdes and Mr. Carpenter today, changing the date from the 9th to the 8th.

Very truly yours, (Signed) David Paine.

DP/MB
Enclosure

[fol. 138] PETITIONERS' EXHIBIT 8.

April 7, 1942.

Honorable Carroll G. Walter, Justice of the New York Supreme Court Chambers, New York County Court House, Foley Square, New York City.

DEAR JUDGE WALTER:

Mr. Carpenter and I deeply appreciate your courtesy in requesting our opinion as to the value of the services rendered by petitioners. We fear however that such an expression of opinion might be construed as a participation in the hearing on the merits and as a waiver of our special appearance, although it is clear that such a result is not contemplated by your courteous request.

In any event, we have no authority as trustees to express an opinion on the matter. Even the federal court under section 62 (a) (c) (d) and 247 of the Bankruptcy Act, cannot fix the amount to be allowed to attorneys for trustees until after various affidavits have been filed and a hearing has been had upon notice to all creditors and stockholders of the debtor, the Securities and Exchange Commission, and such other persons as may be designated by the judge.

All agreements fixing fees in federal reorganization proceedings are unlawful (28 U. S. C. A. 572a). Criminal penalties are imposed for violations.

In order that you may be informed of recent developments, I call your attention to a proceeding which has just been instituted before the United States District Court for [fol. 139] the District of New Jersey by the Trustees for leave to settle, for $150,000, the judgments secured in the New York actions against C. K. Reynolds and William F.

Woodward. A similar proceeding, for leave to settle for $150,000, has also been filed in the United States District Court for the Southern District of New York by Arthur A. Ballantine, as Trustee, for Continental Securities Corporation. The petitions in these proceedings contain information regarding the financial responsibility of the defendants against whom the judgments were rendered.

This letter is not intended as an appearance in the hearing before you, but as a friendly response—outside of the record—to your courteous request.

Copies of this letter are being mailed to the attorneys for the petitioners.

Sincerely yours, (Signed) John Gerdes.

JG:HBH

IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

NOTICE OF MOTION TO RESETTLE ORDER, DATED APRIL 15, 1942

SIRS:

Please take notice that upon the annexed affidavit of John Gerdes sworn to the 21st day of April, 1942, an application will be made to this Court, at a Special Term, Part I thereof, to be held at the New York County Court House, in the Borough of Manhattan, City of New York, on the 27th day [fol. 140] of April, 1942, at 10 o'clock on the forenoon, or as soon thereafter as counsel can be heard, for an order resettling the order signed by Honorable Carroll G. Walter, one of the Justices of this Court, and entered herein on the 15th day of April, 1942; by eliminating the following language in the recitals of said order "and having defaulted in appearing at the adjourned hearing on April 8, 1942" and substituting therefor the language "and said respondents having duly advised the Court and petitioners by letter dated April 7, 1942 that they had no authority from the United States District Court to submit to the general jurisdiction of this Court by participating in the hearing on the merits, and said respondents having failed to appear at the adjourned hearing on April 8, 1942" and

for such other and further relief as to the Court may seem just and proper.

Dated, New York, April 21, 1942.

Yours, etc., John Gerdes, James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Pro Se: One Wall Street, Borough of Manhattan, New York City.

To: Satterlee & Warfield, Esqs., 49 Wall Street, New York City; Greenbaum, Wolff & Ernst, Esqs., 285 Madison Avenue, New York City.

[fol. 141] IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

AFFIDAVIT OF JOHN GERDES, READ IN SUPPORT OF MOTION TO RESETTLE ORDER DATED APRIL 15, 1942

STATE OF NEW YORK,
County of New York, ss:

JOHN GERDES, being duly sworn, deposes and says that he is one of the respondents in the above entitled special proceeding.

Deponent says that on the 7th day of April, 1942 he telephoned to a clerk in the office of Mr. Justice Walter and requested him to tell Mr. Justice Walter that the trustees of Reynolds Investing Company, Inc., were not authorized by the United States District Judge for the District of New Jersey to appear generally before Mr. Justice Walter at the adjourned hearing set for the following day, April 8, 1942, to put in evidence on the merits in this special proceeding. Deponent stated to said clerk that he was mailing a letter to Mr. Justice Walter which would be in the hands of Mr. Justice Walter before the time fixed for the adjourned hearing.

Deponent further states that on said April 7, 1942, the letter, of which a copy is annexed hereto as Exhibit A, was mailed to Mr. Justice Walter, and copies thereof were mailed to Greenbaum, Wolff & Ernst and Satterlee & Warfield, at their respective offices.

(Sworn to April 21, 1942.)

John Gerdes.

[fol. 142] NOTE RE EXHIBIT "A," ANNEXED TO AFFIDAVIT OF JOHN GERDES

This exhibit is identical with Petitioner's Exhibit 8, printed herein at pages 138 and 139.

IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

AFFIDAVIT OF LAWRENCE S. GREENBAUM, READ IN OPPOSITION TO MOTION TO RESETTLE ORDER DATED APRIL 15, 1942

STATE OF NEW YORK,
County of New York, ss:

LAWRENCE S. GREENBAUM, being duly sworn, deposes and says:

I am a member of Greenbaum, Wolff & Ernst, co-petitioners in this proceeding with the members of Kellogg, Emery & Inness-Brown. This affidavit is submitted in opposition to the motion of respondents to resettle the order signed by Hon. Carroll G. Walter and entered herein on the 15th day of April, 1942, by eliminating the recital that respondents defaulted in appearing on the adjourned hearing on April 8, 1942 and substituting a clause to the effect that respondents duly advised the Court that they had no authority to submit to the general jurisdiction by participating on the merits and that they failed to appear at the adjourned hearing.

It is abundantly clear that respondents defaulted and that the recitals in the order properly characterized their conduct and should not be altered.

[fol. 143] In the first place the record establishes that the Federal Bankruptcy Court did in fact authorize respondents to participate on the merits in the instant proceedings and any contrary statement by the respondents is incorrect. As appears from the petition instituting the present proceedings (pp. 15-16 and Exhibit D annexed thereto), petitioners and respondents entered into a stipulation on July 9, 1941 and marked "so ordered" by Judge Fake of the New Jersey Bankruptcy Court on July 10, 1941 providing that the petitioners herein would commence proceedings in the State courts of New York for the fixa-

tion of their liens. The stipulation further reserved the right to respondents to question the jurisdiction of the New York courts. In other words, the Federal Bankruptcy Court expressly authorized the commencement of these proceedings, and this authorization coupled with the reservation to respondents of the privilege if they desired to raise a jurisdictional question obviously included the authority to proceed on the merits as well.

In the second place, assuming that no express authority to participate on the merits in these proceedings existed, the respondents nevertheless committed a default after the New York Court held that jurisdiction existed to determine and fix petitioners' liens and by its intermediate order entered on March 27 set down the matter for hearing upon the merits.

The decision and intermediate order of Mr. Justice Walter holding that the New York Court had jurisdiction was predicated upon the fact that the Federal Bankruptcy Court by explicit order authorized the institution of the litigation in New York with respect to which petitioners [fol. 144] herein sought to fix and determine their liens. The respondents having thus voluntarily become active litigants in the courts of New York with petitioners as their attorneys, they thereby submitted themselves to the jurisdiction of the New York court respecting all incidents of the litigation including the right in rem under the New York judiciary law to fix and determine petitioners' liens. The question whether the Bankruptcy Court did or did not authorize respondents to participate on the merits in the proceeding to fix the lien is consequently of no moment since jurisdiction to fix and enforce such liens attached by the antecedent conduct of instituting the litigation in New York with the approval and authority of the Bankruptcy Court. This Court having signed the intermediate order overruling the jurisdictional objection raised by respondents and setting the matter down for hearing on the merits, the refusal of respondents to proceed and their failure to appear at the adjourned hearing after due notice constituted a clear default.

It is respectfully submitted that the motion to resettle the order entered April 15, 1942 be denied in all respects.

Lawrence S. Greenbaum.

(Sworn to April 24, 1942.)

[fol. 145] In Supreme Court of New York, New York County

Opinion of Walter, J., on Order Overruling Respondents' Objections to Jurisdiction of the Court

(The New York Law Journal, Friday March 6, 1942.)

P. 987

[Matter in italics so in original]

New York attorneys here ask the court to fix and enforce a lien in their favor for services performed by them as attorneys for the plaintiffs in three action- brought in this court. Their clients are trustees in bankruptcy who make what they call a special appearance for the purpose of contesting the jurisdiction of the court, their contention being that only the bankruptcy court which appointed them has jurisdiction to grant the relief sought.

A petition for reorganization of Reynolds Investing Company, a Delaware corporation, under the Federal Bankruptcy Act was filed on May 18, 1938, in the United States District Court for the District of New Jersey. That court, on August 1, 1938, authorized the company to commence an action in this court and for that purpose to retain the petitioners herein, and such action was so brought [fol. 146] on August 4, 1938. That court later appointed trustees of the company, and in its order of appointment authorized them to become parties to and to prosecute that action, and such trustees were later substituted for the company as parties plaintiff in such action by order of this court made upon their application. Those trustees also later brought two other actions in this court, one on January 16, 1940, and the other on May 29, 1940, the petitioners herein acting as their attorneys pursuant to retainer by them authorized by the bankruptcy court. The action first brought was tried and resulted in a favorable final judgment as to some matters and a reference as to others (*Gerdes* v. *Reynolds*, 28 N. Y. Supp. 2d, 622). The other two actions have not yet been tried and are still pending undetermined.

In June, 1941, while the reference was pending, the trustees, who themselves are lawyers, one of New York and the

other of New Jersey, notified their attorneys that they would take over the litigation, with the exception that they would expect the attorneys to conclude the hearings before the referee. Such notification was not because of any misconduct on the part of the attorneys. The attorneys replied that they were prepared to accede to the trustees' wishes provided they were relieved of their responsibilities and their fees and disbursements to date were paid. The trustees thereupon petitioned the bankruptcy court for an order requiring the attorneys to turn over all papers and fixing the amount of their fees and disbursements. The attorneys protested that the fixing and enforcement of their liens for [fol. 147] services were matters for determination by this court, and after some argument before the bankruptcy court the trustees withdrew their application to that court under a stipulation which, after various provisions respecting use of papers, provided that respondents should make this present application to this court and that both sides respectfully reserved the right to question the jurisdiction of each court. That stipulation was approved by the bankruptcy court by the judge thereof endorsing thereon the words "so ordered." That court thus in effect authorized this proceeding subject to the trustees' claim of lack of jurisdiction.

I am of the opinion that the short, simple, conclusive and all sufficient answer to the contention of the trustees is that first the bankrupt and then they themselves, both with the approval and by the direction of the bankruptcy court, voluntarily became active litigants in this court with petitioners as their attorneys, and they thereby submitted themselves to the jurisdiction of this court respecting all incidents of that litigation, and they cannot avoid such submission by the device of discharging their attorneys even though they refrain from formally moving for the substitution which they in effect seek. Asserting a claim in a court is a waiver of immunity from its process at least as to that claim and its incidents (*Sherman* v. *Buckley*, 119 Fed. [2d], 280; *The Davis*, 10 Wall. 15; *The Siren*, 7 Wall. 152; *United States* v. *The Thekla*, 266 U. S. 328, 339, 340; *In re United States Steel Products Co.*, 24 Fed. [2d], 657, 659; *United States* v. *Shaw*, 309 U. S. 495).

[fol. 148] The question, however, is not only practically important, but also has all the delicacy inherent in all questions involving possible conflicts of jurisdiction, and having

been in effect referred by the bankruptcy court to this court I think it proper that full consideration be given to the precise nature of attorneys' liens as well as of the oft-asserted exclusiveness of the jurisdiction of courts in bankruptcy over the property of the bankrupt.

Under the New York law an attorney in the absence of contract to the contrary, has two well-defined rights, which go by the names of a retaining lien and a charging lien. The retaining lien is a right to retain possession of all papers, securities, or moneys belonging to his client, which came into his possession in the course of his professional employment until he is paid whatever is due him for any and all services rendered for the client; and the charging lien is a right to have the proceeds of his client's claim or cause of action applied to the payment of his charges for services rendered in connection with that claim or cause of action (*Goodrich* v. *McDonald*, 112 N. Y. 157, 162-165; *Matter of Heimsheimer*, 214 N. Y. 361, 364, 365). Both liens existed at common law, with the exception that at common law the charging lien did not arise until judgment was recovered, whereas under the statute which is now Section 475 of the Judiciary Law it exists upon the cause of action from the commencement of the suit or proceeding for the enforcement thereof (*Matter of Heinsheimer, supra*, at p. 365; *Beecher* v. *Vogt Mfg. Co.*, 227 N. Y. 468, 471). If the at-[fol. 149] torney give cause for his discharge by the client, or if without just cause he refuse to proceed with his client's case, he forfeits his lien (*Matter of Montgomery*, 272 N. Y. 323, 326; *Holmes* v. *Evans*, 129 N. Y. 140; *Matter of Dunn*, 205 N. Y. 398, 401). The client, on the other hand, has an absolute right to discharge his attorney without cause at any time, the personal and confidential nature of the relationship of attorney and client having caused the courts of this state to treat such right to discharge without cause as an implied term of every contract of retainer (*Martin* v. *Camp*, 219 N. Y. 170; *Matter of City of N. Y.*, 219 N. Y. 192; *Matter of Krooks*, 257 N. Y. 329, 331; *Matter of Hillman*, 259 N. Y. 133, 135; *Matter of Lydig*, 262 N. Y. 408, 409; *Matter of Weitling* 266 N. Y. 184, 186). But while a client who exercises that right to discharge his attorney without cause does not make himself liable for damages for breach of contract (*Martin* v. *Camp; supra*), and is entitled to immediate substitution of a new attorney (*Mater of Lydig, supra*), he thereby cancels the contract of retainer and en-

titles the discharged attorney to immediate payment of the reasonable value of the services rendered by him to the time of the discharge (*Matter of Krooks, supra; Matter of Tillman, supra; Matter of Weitling, supra; Matter of Montgomery, supra*). Quantum meruit, and not the contract of retainer, then becomes the measure of the attorney's immediate right, regardless of whether the retainer was on a contingent basis (*Matter of Krooks, supra; Matter of Tillman, supra; Matter of Weitling, supra*), or for stated sum (*Matter of Montgomery, supra*).

[fol. 150] A client has absolute power to make an honest and good faith settlement of his case, even though he has contracted with his attorney for a contingent fee of a percentage of the amount recovered, the attorney's lien being then imposed upon the proceeds of the settlement (*Matter of Levy*, 249 N. Y. 168), but subject to the client's right to settle the attorney is regarded as in the position of an equitable assignee of the client's claim (*Beecher* v. *Vogt Mfg. Co.*, 227 N. Y. 468, 472; *Matter of Levy, supra*, at p. 171), and the essence of the right which now goes under the name of a charging lien is a right to have the court exercise in the attorney's favor the control which the court has of its judgments and records and of the means of enforcing its judgment (*Goodrich* v. *McDonald*, 112 N. Y. 157, 164, 165). Under some circumstances the attorney may bring an action to enforce his lien (*Fischer-Hansen* v. *Brooklyn Heights RR.*, 173 N. Y. 492), but the usual and customary as well as the historical method of enforcement is an application to the court in which the client's action was brought (*Goodrich* v. *McDonald, supra*, at pp. 163-166). Sometimes such application takes the form of a proceeding to vacate a satisfaction of the judgment and permit enforcement thereof to the extent of the attorney's lien (*Peri* v. *N. Y. Central RR.*, 152 N. Y. 521, 522; *Matter of Regan*, 167 N. Y. 338). At other times it takes the form of a petition by the attorney to fix the value of his services (*Matter of King*, 168 N. Y. 53; *Matter of Fitzsimons*, 174 N. Y. 15). At still other times the lien is fixed as an incident of an application by the client for a substitution of attorneys or to compel a turning over of papers (*Matter of Krooks*, 257 N. Y. 329; [fol. 151] *Matter of Tillman*, 259 N. Y. 134; *Matter of Weitling*, 266 N. Y. 184). In a procedural sense, such applications by attorneys, whether entitled in the client's action or not, are regarded as separate special proceedings

rather than as proceedings in the client's action (*Peri* v. *N. Y. Central RR., supra; Matter of Regan, supra; Matter of King, supra*, at p. 60; *Matter of Fizsimons, supra*; at p. 20), but the important fact is that they are made to the court in which the client's action or proceeding was brought and in which the attorney's services were rendered, and that such court has been expressly held to have jurisdiction thereof even where the client was an administrator appointed by and accountable to another court (*Matter of Atterbury*, 222 N. Y. 355), or even a trustee acting under appointment in another state (*Matter of King, supra*, at pp. 59, 60).

Two things are thus conspicuously manifest: First, that an attorney discharged without cause thereby becomes immediately entitled to payment of the reasonable value of the services rendered to the date of his discharge, irrespective of the terms of the contra . by whi h he was retained, and, second, that he is entitled i inv the process of the court in which was or is pending t ..on or proceeding in which he rendered his services to obtain such payment before his client gets the proceeds of the judgment or settlement which the attorney's efforts have brought about. In other words, to repeat, the thing we call a lien is a right to have that court so control its own judgments and processes as to see that the attorney is paid before the client gets the recovery into his own hands (see, again, *Goodrich* v. *McDonald*, [fol. 152] *supra*, and *Matter of King, supra*). As was said in those cases, the attorney's lien is a peculiar lien, to be enforced by peculiar methods, and was never enforced like other liens.

Enforcement, however, is the attorney's right, and the court has no jurisdiction to free from the lien property which the statute declares is subject to it (*Robinson* v. *Rogers*, 237 N. Y. 467, 472, 473), even to the extent of decreeing a setoff against the client's cause of action (*Beecher* v. *Vogt Mfg. Co.*, 227 N. Y. 468). Fixation, at least, there must be (*Matter of Tillman, supra; Matter of Krooks, supra; Bernstein* v. *Bedrick*, 262 N. Y. 472, 473), and while there may be some uncertainty as to whether or not papers may be ordered turned over to the client, with consequent destruction of the retaining lien, without actual payment of the attorney's charges, it is certain that as to the charging

lien "the courts cannot themselves substitute another form of protection for that provided in the statute" (*Robinson* v. *Rogers, supra,* at p. 472).*

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*No application to compel the turning over of papers is presently before the court and no definite adjudication need now be made, but it is not out of place to note the decisions with reference thereto.

The Court of Appeals several times has intimated that the turning over of papers may be ordered when the attorney's fees are fixed and either *paid or secured* (*Matter of Dunn,* 205 N. Y. 398, 401; *Robinson* v. *Rogers,* 237 N. Y. 467, 471; *Bernstein* v. *Bedrick,* 262 N. Y. 472, 473), but it also has stated that upon discharge the attorney is entitled to be *paid,* and that the client can discharge the attorney only "upon *payment* for services rendered" (*Matter of Weitling,* 266 N. Y. 184, 186). The view that the giving of adequate security is sufficient was taken by the Appellate Division of the Fourth Department in *Matter of Makames* (238 App. Div. 534, 537), and *Gurecki* v. *Bush* (254 App. Div. 813, 814). The decision of the Second Department in *Matter of Korn* (255 App. Div. 870, 871) seems to take the view that payment in cash is essential. In *Matter of McNally* v. *Youngs* (237 App. Div. 787, 188) the First Department interpreted *Robinson* v. *Rogers* (supra) as requiring payment as a condition of turning over papers, and also as a condition of granting substitution, but that decision was rendered before *Matter of Lydig* (262 N. Y. 408), and *Bernstein* v. *Bedrick* (supra), and in the later case of *Fitzsimmons* v. *Long Island Lighting Co.* (251 App. Div. 395, 399), the First Department held that it was error to make substitutions conditional upon payment, and also held, upon the authority of *Robinson* v. *Rogers* (supra), without citing *Matter of Weiling* (supra) that papers may be ordered turned over upon either payment or the furnishing of proper security.

The client's "pressing necessity" for papers in the attorney's possession frequently has been put forward as a ground for compelling their delivery to him (see, for example, *Matter of Makames,* 238 App. Div. 534, 537), but in *Matter of Weitling* (266 N. Y. 184, 186, 187) the Court of Appeals expressly stated, "In the absence of such payment

[fol. 153] The attorneys' liens as thus developed in New York are not mere regulations of practice of its courts. They are substantive rights which the federal courts recognize and enforce, and it is settled that they are not displaced or invalidated by the bankruptcy of the client (*In re Baxter & Co.*, 154 Fed. 22, 25; *In re Badger*, 9 Fed. 2d 560; *In re San Juan Gold, Inc.*, 96 Fed. 2d 60; *In re Prudence Co., Inc.*, 96 Fed. 2d 167, 160; *Nic Projector Corp'n.* v. *Movie-Jecker Co.*, 16 Fed. Supp. 605; *Lawrence* v. *Commodore Nav. Corp'n.*, 27 Fed. Supp. 139). The federal courts further hold that the suit upon which the lien exists (the suit in which the attorney's services were rendered) cannot be terminated or finally disposed of without fixing the attorney's lien, and that a proceeding to fix the lien is so strictly ancillary to that suit that federal jurisdiction of such a [fol. 154] proceeding exists even though there be no such diversity of citizenship between the parties to such proceeding as would support federal jurisdiction of the fixation proceeding apart from the court's jurisdiction over the client's suit—and that, too, even though no substitution of attorneys in the client's suit is asked (*Woodbury* v. *Jergens Co.*, 69 Fed. 2d 49; *Lawrence* v. *Commodore Nav. Corp'n*, *supra*). In strikingly emphatic fashion, therefore, the federal courts also recognize the essential nature of the attorney's charging lien as being, as I have stated above, a right in the attorney to have the court in which the client's suit was brought so to control its own judgments and processes as to see that the attorney is paid before the client gets any recovery into his own hands (see also *Tuttle* v. *Claflin*, 88 Fed. 122, 124, 125, holding that an attorney's lien upon

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the retaining liens remains in force and the attorney cannot be compelled to surrender the papers in relation to the action in his possession, in the absence of unprofessional conduct on his part," and it hardly can be said that it is unprofessional conduct for an attorney to insist upon a lien which the law gives him. It repeatedly has been recognized that the lien is valuable in proportion as denial of access to the papers causes inconvenience to the client, and that the lien cannot be disdegarded merely because the pressure it is supposed to exert becomes effective (*In re San Juan Gold, Inc.*, 96 Fed. 2d 60), which so held even upon an application to compel the turning over of papers needed in a bankruptcy reorganization.

[fol. 155] a recovery should be fixed before it is turned over to an assignee for the benefit of creditors in another jurisdiction).

That being the essential nature of an attorney's charging lien it would seem to follow that, despite the bankruptcy of the client, the power to fix and enforce the lien still must remain in the court in which the client's suit was brought; but even if that result do not follow from the nature of the lien alone there are still other reasons why the bankruptcy of the client does not cause the power to fix and enforce the lien to pass from that court to the bankruptcy court.

The rule that the bankruptcy court has exclusive jurisdiction to deal with the property of the bankrupt estate is but an application of the broader rule that when a court of competent jurisdiction takes possession of property for the purpose of administering it no other court can then interfere with or disturb that possession (*Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 737), which is a rule I myself recently have had occasion to enforce (*City of N. Y.* v. *Darlington*, 177 Misc. 87, 90), and when a state court at the time bankruptcy occurs already is proceeding to ascertain and enforce existing liens of a kind not invalidated by the bankruptcy, that identical rule requires, and has evoked the holding that the bankruptcy does not oust the state court of its jurisdiction or vest the bankruptcy court with power to enjoin its proceedings (*Straton* v. *New*, 283 U. S. 318, and see also *Metcalf* v. *Barker*, 187 U. S. 165, which is particularly apposite because it related, in part, to a lien which, [fol. 156] like an attorney's charging lien, was acquired by the commencement of a suit).

It consequently would seem that, as an attorney's lien dates from the commencement of the client's action and is one of a kind not invalidated by bankruptcy, and as an application by a discharged attorney for enforcement of such lien is, in substance though not necessarily procedurally, an application to the court in which that action is or has been pending to exercise its own existing power over its own judgments and processes, it is that court which is to be regarded as having first taken possession of the property involved (the client's cause of action) and the court which is to retain that possession free from the interference of any other court.

The assertion that by the filing of a petition in bankruptcy the property of the bankrupt is placed in the custody

of the bankruptcy court (*Straton* v. *New, supra,* at p. 321), when applied to a liability or chose in action as distinguished from tangible real or personal property, is at best the assertion of a legal concept based upon the court's power over a person (see cases cited in *Sherman* v. *Buckley,* 119 Fed. 2d 280, 282, first column), and while I concede both the utility and effectiveness of the concept under certain circumstances I do not think it can prevail when it collides with the equally well-founded concept that when the cause of action was made the basis of a suit in a court it came into the custody of that court.

If in ascertaining and enforcing an attorney's lien the court in which the client's cause of action is asserted were making a general disposition and distribution of all the [fol. 157] bankrupt client's property, or generally marshaling all liens and claims upon all such property, then, of course, bankruptcy, necessarily would halt its proceedings (*Straton* v. *New, supra,* at p. 327), but in so ascertaining and enforcing the lien it is doing nothing of that sort. In so doing it is merely determining what part of one item of the bankrupt client's property remained vested in him after the commencement of the action made the attorney therein the equitable and statutory assignee of some fraction of that one item of property, and it is only the part which so remained vested in the bankrupt client which ever became subject to administration in bankruptcy (compare the recognition in *In re Borok,* 50 Fed. 2d 75, 77, and in *In re Worrall,* 79 Fed. 2d 88, 90, 91, that a transfer which destroys the bankrupt's title to or control over a chose of action, such as an assignment of which the debtor is notified, prevents such chose in action from coming into the "possession" of the bankruptcy court).

In point of fact, moreover, the bankruptcy courts themselves recognize that causes of action which the bankrupt is prosecuting by means of a suit do not come into the custody or possession of the bankruptcy court by the mere fact of the filing of the petition or of the adjudication. A trustee in bankruptcy does not by the mere fact of his appointment become a party to every lawsuit in which the bankrupt is plaintiff, and the mere fact of bankruptcy does not operate as a stay. Unless the trustee take some affirmative action the suit may proceed as if bankruptcy had not intervened (Bankruptcy Act, section 11, sub-division (c); 11 U. S. Code, sec. 29; Collier on Bankruptcy, 14th ed., paragraph

[fol. 158] 11.10; *In re Prudence Co., Inc.*, 96 Fed. 2d 157), and where the trustee allows the bankrupt to continue prosecution of a pending suit through his own attorney that attorney's contract of retainer is not canceled, and he is entitled to the fee stipulated therein (*In re Prudence Co., Inc.*, 96 Fed. 2d 157). That that is so demonstrates, I think, not only that the trustee's title to a cause of action which is being asserted in a lawsuit is subject to the attorney's lien, but also that such a cause of action affords at least one instance, where even under the Bankruptcy Act, the trustee's acquisition of title does not draw with it even the constructive possession which sometimes suffices as a basis for an exercise of summary jurisdiction by the bankruptcy court.

It is, indeed, little short of an absolute contradiction to say that a bankruptcy court has possession of something which the trustee must go into another court in order to get. If, however, causes of action being prosecuted by the bankrupt by means of a suit were to be regarded as coming into the possession of the bankruptcy court by the mere fact of the filing of the petition or of the adjudication, that still would not exclude the jurisdiction of this court in this case.

Even where the jurisdiction of the bankruptcy court is exclusive, it is exclusive "save by consent of the Bankruptcy Court" (*Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 739), and not only is it common practice for the bankruptcy court to permit state courts to exercise jurisdiction where it could prevent such exercise (*In re Schulte United, Inc.*, 49 Fed. 2d [illegible]4), but there also appears a growing tendency (to be accelerated no doubt by *Erie R. R.* v. [fol. 159] *Tompkins*, 304 U. S. 64), to regard it as an abuse of discretion to refuse to permit such exercise where local rights or questions are involved and there is no actual interference with or encumbrance upon bankruptcy administration (*Foust* v. *Munson S. S. Lines*, 299 U. S. 77, 86; *State of Texas* v. *Donoghue*, 302 U. S. 284; *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478). In the case last cited the word "nondelegable" was used in connection with the statement of the bankruptcy court's exclusive control over the administration of an estate in its possession (p. 483), but that word was not used as meaning that the bankruptcy court may not permit the determination of rights to or against property in its possession by litigation in the state courts is demonstrated by the fact that in that very case the

bankruptcy court was reversed because it had refused to permit such determination by means of a suit in a state court.

The bankruptcy court thus may and sometimes should permit state courts to determine rights and questions affecting property which is either actually or constructively in its possession, and where, as here, the bankruptcy court has authorized the institution of actions in this court, and the trustees have become litigants in this court through attorneys authorized by them and by the bankruptcy court, there can be no doubt of the jurisdiction of this court to carry the litigation through to its end, including the incident of fixing and enforcing the attorney's lien (*Sherman* v. *Buckley*, 119 Fed. 2d 280; *Ohio Oil Co.* v. *Thompson*, 120 Fed. 2d 831, 836, second column). Choice was made when the trustees became parties to the litigation in this court. [fol. 160] They cannot revoke that choice now.

The trustees urge that by various orders and by its approval of a plan of reorganization the bankruptcy court has enjoined the commencement or continuance of any judicial proceeding to enforce any lien upon the estate of the bankrupt, that it also has reserved the power to fix the compensation of the trustees and their attorneys, and that by their participation in the formulation and adoption of the plan of reorganization the petitioners herein have in effect agreed to abide by the plan and to look for their compensation to such allowance as the bankruptcy court shall make. It is quite doubtful, I think, whether any of the provisions involved by the trustees go any further than what would be true under the law without them, but whether that be so or not it is entirely clear that they cannot be given the effect contended for by the trustees.

The clause respecting proceedings to enforce liens is of general application and cannot be so read as to contradict the specific action of the court in authorizing the institution and prosecution of the suits in this court by the trustees through these petitioners as their attorneys (compare *In re Prudence Co., Inc.*, 96 Fed. [2d] 157, 159, 160). In like manner, the clause respecting fixation of fees by the bankruptcy court obviously applies to fees for services in the bankruptcy proceeding, and cannot be read as having application to fees for services in the actions which the court authorized to be brought in this court (compare *Palmer* v. *Larchmont Manor Co.*, 284 N. Y. 288). The participation

[fol. 161]of these petitioners in the bankruptcy proceeding was, in part at least, as attorneys for parties other than the trustees, and they have made no request that this court either fix or allow any fee for those services. Finally, if there be any ground for saying that any act of petitioners constituted an implied agreement by them to look to the bankruptcy court for an allowance for their services in the actions in this court, as distinguished from an allowance for services rendered in the bankruptcy proceeding itself, such implied agreement was canceled and terminated when the trustees discharged them (see *Matter of Krooks*, *Matter of Tillman*, *Matter of Weitling* and *Matter of Montgomery*, all hereinabove cited), and it must here be assumed, in view of the position taken by the trustees before this court, that such discharge of petitioners by the trustees was authorized by the bankruptcy court with knowledge and appreciation of the consequences of such discharge.

Palmer v. *Larchmont Manor Co.* (284 N. Y. 288), which has been cited by the trustees has not been overlooked. What is there held is that a state court has no jurisdiction of a suit by trustees in bankruptcy unless the bankruptcy court consents to its institution, and that such consent must be pleaded and must be specific enough to authorize the particular suit which is brought. Here it is undisputed that the bankruptcy court specifically gave authorization to bring in this court the three suits which were so brought. The only feature of the case cited which is pertinent here is the approval there given to the principle I already have applied [fol. 162] that as a rule general language in orders of a court ought not to be construed as covering specific situations not apparently within the contemplation of the court when the order was made.

The objection to the jurisdiction of the court is overruled. If the trustees desire to answer further with respect to the merits they may do so within ten days after publication of this opinion. An order specifying the mode of trial upon the merits may then be settled upon notice.

IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

OPINION OF WALTER, J. ON ORDER FIXING LIEN AND AMOUNT OF ATTORNEYS' COMPENSATION

Walter, J.: This is a proceeding by New York attorneys for a fixation and enforcement of their lien for services in

three actions in this court in which they represented respondents.

In an opinion published in the New York Law Journal of March 6, 1942, page 987, I overruled respondent's objection to the jurisdiction of the Court and gave them leave to answer upon the merits. Respondents did not elect to answer farther, and I then made an order setting the proceeding down for hearing upon the merits on March 31, 1942. On that day petitioners stated that they were ready to proceed, and respondents asked that the hearing be stayed or adjourned pending the determination of a petition by them for an order prohibiting me from proceeding. Their petition for such order (which was then served upon me along with a notice of motion to be made by them in the Appellate [fol. 163] Division on April 17, 1942) contained the statement that application had been made to the Appellate Division for an order to show cause, returnable on April 2, 1942, and containing a temporary stay, and that such application had been denied. The Appellate Division having thus denied an application for a stay, I refused respondents' request for a stay or adjournment of the hearing then in progress before me, and announced that I would proceed with the taking of evidence. Respondents then stated that they would take no part in the hearing, and their representative actually left the courtroom. Petitioners then introduced their evidence.

When they had rested I of my own motion adjourned the matter to April 9, 1942 (a date later changed to April 8, 1942, at petitioners' request) and I stated that I would then hear any evidence respondents then cared to present and directed petitioners to so notify respondents, who then, as stated, had absented themselves from the courtroom. I did that in the hope that respondents would reconsider their course and give the Court the benefit of their views respecting the reasonable value of petitioners' services.

On the adjourned date, however, respondents again declined to attend or appear.

If there were any doubt as to the right of the litigant to participate in a hearing upon the merits after his objection to jurisdiction is overruled, without thereby waiving his objection to jurisdiction or his right to review by appeal the overruling thereof, the attitude of respondents would be quite understandable, but such right has been often reiterated in both State and Federal decisions (*Avery* v. *Slack*,

[fol. 164] 17 Wend. 85; *Jones* v. *Jones*, 108 N. Y. 415, 425; *Allen* v. *Gray*, 201 N. Y. 504; *Muslusky* v. *Lehigh Valley Coal Co.*, 225 N. Y. 584, 587, citing *Toledo Rys. & Light Co.* v. *Hill*, 244 U. S. 49; *Finsilver, Still & Moss* v. *Goldberg M. & Co.*, 253 N. Y. 382, 391; *Fickett* v. *Higginbotham-Bailey-Logan Co.*, 162 Misc. 18, 19; *Toledo Rys. & Light Co.* v. *Hill*, 244 U. S. 49; *Harkness* v. *Hyde*, 98 U. S. 476; *Hassler* v. *Shaw*, 271 U. S. 195; *Baldwin* v. *Traveling Men's Association*, 283 U. S. 522, 525).

As the right is thus well settled, and as that fact was called to respondents' attention by me before they absented themselves from the hearing, even to the extent of referring them specifically to *Toledo Rys. & Light Co.* v. *Hill*, 244 U. S. 49, I find it difficult to ascribe their refusal to participate in the hearing upon the merits to any genuine fear that such participation might prejudice their position upon the question of jurisdiction. Rather, I think, they put themselves in a position which justifies application of the rule that all evidence is to be weighed according to the proof which it is in the power of a party to produce (*Layer* v. *City of Buffalo*, 274 N. Y. 135, 140) and that as against a party who omits to speak every inference warranted by the evidence should be indulged (*Wylde* v. *Northern R. R. Co.*, 53 N. Y. 156, 164).

The Court accordingly now proceeds, through no choice of its own, to determine the reasonable value of petitioners' services upon the record as it stands.

Two of the actions in which petitioners rendered services, those designated in the record as Actions Numbers 2 and 3, have not been tried, and have resulted in no benefit to [fol. 165] their clients, and it seems highly problematical that they ever will be tried or that, if tried, they will actually yield more than a small financial return. Nevertheless, work actually necessarily was performed with respect to them and they presented substantial questions of law and fact and some actual benefit reasonably may be expected, and I find and decide that the reasonable value of the services rendered in Action Number 2 is $2000 and that the reasonable value of the services rendered in Action Number 3 is $750. Petitioners are accordingly declared to have a lien upon the causes of action asserted in those two actions for those amounts respectively.

The other action in which petitioners rendered services, that designated in the record as Action Number 1, is the

one which was tried before me, and the nature of it is fully disclosed in my opinion therein and in the report of the referee and in my opinion confirming that report (*Gerdes* v. *Reynolds*, 28 N. Y. Supp. 2nd 622, and 30 N. Y. Supp. 2nd 755).

Considering solely the time reasonably and necessarily spent upon the case, the difficulties involved, the nature of the services, the skill employed, the amount involved, the standing of the attorneys engaged upon the case, and the place where the services were rendered (*Matter of Potts*, 213 App. Div. 59, 62, *Straus* v. *Victor Talking Machine Co.*, 297 Fed. 791, 805, 806; *Taylor* v. *Scarborough*, 66 Fed. 2nd 589; *Rogers* v. *Hill*, 34 Fed. Supp. 358, 363; *In re Osofsky*, 50 Fed. 2nd 925, 927; *Irwin* v. *Swinney*, 45 Fed. 2nd 890, 893). I would have no hesitation in finding and deciding that the reasonable value of the services rendered in that Action [fol. 166] Number 1 is the amount stated by petitioners in their testimony, namely, $145,000. A considerably larger sum undoubtedly would be justified if the judgments obtained in the action were wholly collectible. Another element to be considered, however, is the result obtained, and I think it plain that *is* what is meant by "result obtained" is the actual benefit to the client rather than the size of the judgment entered (*Randall* v. *Packard*, 142 N. Y. 47, 57; *Rogers* v. *Hill*, 34 Fed. Supp. 358, 363). "A judgment for a sum of money is only a trophy of an empty victory unless it is collected" (*Matter of Auditore*, 278 N. Y. 234, 240) and financial ability of the debtor to pay a large judgment obviously must be taken into account.

I do not mean to say that if a client engages an attorney to prosecute a difficult and complicated claim for $1,000,000 and the attorney is successful after long effort in recovering a judgment for that amount the attorney should be awarded nothing because the judgment proves uncollectible. All that I say is that the real, rather than the nominal, result to the client is an element to be considered in fixing reasonable value.

On the other hand, the principle that it is the real benefit to the client that is to be considered, rather than the size of the judgment entered, necessarily leads to the conclusion that a benefit in addition to the judgment should be taken into the reckoning if such benefit be properly proved with reasonable certainty. (Compare *Wakeman* v. *Wheeler &*

Wilson Mfg. Co., 101 N. Y. 205, as to recovery of prospective profits on breach of contract.)

[fol. 167] It therefore is here proper to take into consideration the fact that the work done by petitioners in Action Number 1 will be of benefit to respondents in a case which respondents are prosecuting in Virginia against parties who were named as defendants in that action, but against whom a separate suit had to be brought in Virginia because those parties could not be served with process here. Not only will respondents get in the Virginia action the benefit of the facts and law examined by petitioners in the action already tried here, but it is even testified that arrangements have been made that the evidence taken in the action here may be used in the Virginia action.

Taking that benefit into consideration does not in any way involve giving petitioners a lien upon the cause of action tried here for services rendered in the Virginia action. It merely means that the entire benefit which respondents derived from the services rendered in the action tried here are taken into consideration in fixing the reasonable value of such services.

Considering that benefit, I am constrained to reduce the sum which I would otherwise fix, and I accordingly find and decide that the reasonable value of the services rendered by petitioners in Action Number 1 is $100,000. Petitioners are accordingly declared to have a lien for that amount upon the causes of action asserted and the judgments obtained in Action Number 1.

In each instance, petitioners are entitled to interest upon the respective amounts herein specified from November 27, 1941, when their services terminated and payment to them became due (*Adams* v. *Fort Plain Bank*, 36 N. Y. 255; [fol. 168] *Blackwell* v. *Finlay*, 233 N. Y. 361; *Prager* v. *New Jersey Fidelity & Plate Glass Ins. Co.*, 245 N. Y. 1; *Preston* v. *Funkhouser*, 261 N. Y. 140; *Taylor* v. *Scarborough*, 66 Fed. 2nd 589, 592).

Settle final order accordingly on two days' notice.

In the event of any appeal from such final order, appropriate provision will be made in accordance with the rules whereby the part of the record to be printed will be reduced to a minimum.

[fol. 169] AFFIDAVIT OF NO OTHER OPINION ON ORDER DENYING MOTION TO RESETTLE ORDER DATED APRIL 15, 1942

STATE OF NEW YORK,
County of New York, ss.:

Irving T. Bush, being duly sworn, says:

I am an attorney-at-law, associated with John Gerdes, one of the Trustees and attorneys pro se, one of the respondents-appellants in this proceeding and am familiar with all the proceedings herein.

No opinion was delivered by the Court below in making the order denying the motion to resettle the order dated April 15, 1942 appealed from except as appears therein, which order is printed herein at pages 15 and 16.

Irving T. Bush.

Sworn to before me this 1st day of June, 1942. William C. Porth, Attorney and Counsellor-at-Law. New York Co. Clk's No. 8, Reg. No. 4 P 179. Office & P. O. Address, 1 Wall St., N. Y. City. Commission expires March 30, 1944.

[fol. 170] IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

[Title omitted]

STIPULATION AS TO EXHIBITS—May 29, 1942

[fol. 171] It is herely stipulated and agreed that Exhibit A, Annexed to Petition of B. H. Inness Brown, et al., totaling 134 typewritten pages consisted of a summary statement of services rendered, based on diary entries be and the same hereby is omitted from the printed record and that a statement be printed in lieu thereof.

It is further stipulated and agreed that the following Petitioners' Exhibits:

2—Judgments entered in Suit No. 1;

3—Files from office of County Clerk of New York in regard to this case; and

4—Stenographer's minutes of trial in case of Gerdes, et al. v. Reynolds, et al.

which were received and marked in evidence at the hearings before Hon. Carroll G. Walter, on value of services, be and the same are hereby omitted from the printed record and that a statement be printed in lieu thereof.

It is further stipulated and agreed that these exhibits may be handed up on the argument of this appeal with the same force and effect as though incorporated herein.

Dated, New York, May 29, 1942.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants, Pro se. Satterlee & Warfield and Greenbaum, Wolff & Ernst, Attorneys for Petitioners-Respondents.

So ordered. F. M.

[fol. 172] In Supreme Court of New York, New York County

Stipulation Settling Case—June 1, 1942

It is hereby stipulated by and between the attorneys for the respective parties hereto that the foregoing case contains all the evidence taken upon the trial and all exceptions of all parties and that an order may be entered herein settling the same as such and ordering the same on file without further notice.

Dated, New York, June 1, 1942.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants, Pro se. Satterlee & Warfield and Greenbaum, Wolff & Ernst, Attorneys for Petitioners-Respondents.

In Supreme Court of New York, New York County

Order Settling Case

On the foregoing stipulation the above case on appeal which contains all the evidence and exceptions of all parties is hereby settled and ordered on file.

Dated, New York, June —, 1942.

Carroll G. Walter, J. S. C.

[fols. 173-174] IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

STIPULATION WAIVING CERTIFICATION—June 1, 1942

It is hereby stipulated by and between the attorneys for the respective parties hereto that the foregoing are true copies of the notices of appeal, the orders appealed from and all the papers used before the Court below in making the orders appealed from herein, the case and exceptions as settled and the whole thereof now on file in the office of the Clerk of the County of New York and that certification thereof is hereby waived and that an order directing the filing of the record in the Appellate Court may be entered without further notice.

Dated, New York, June 1, 1942.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants, Pro se. Satterlee & Warfield and Greenbaum, Wolff & Ernst, Attorneys for Petitioners-Respondents.

IN SUPREME COURT OF NEW YORK, NEW YORK COUNTY

ORDER FILING RECORD IN APPELLATE DIVISION

Pursuant to the foregoing stipulation, it is ordered that the foregoing printed record be filed in the office of the Clerk of the Appellate Division of the Supreme Court, First Judicial Department.

Dated, New York, June —, 1942.

Carroll G. Walter, J. S. C.

[fol. 175] IN NEW YORK SUPREME COURT, APPELLATE DIVISION, FIRST DEPARTMENT

[Title omitted]

NOTICE OF APPEAL TO COURT OF APPEALS—August 17, 1942

[fol. 176] SIRS:

Please take notice that John Gerdes and James D. Carpenter, Jr. as Trustees of Reynolds Investing Co. Inc.,

Debtor, the above named respondents-appellants, hereby appeal to the Court of Appeals from the final order of the Appellate Division of the Supreme Court for the First Department, entered in the office of the Clerk of said Court on the 19th day of June, 1942, affirming the orders of the Special Term of the Supreme Court, New York County, entered in the office of the Clerk of the County of New York on the 27th day of March, 1942, the 15th day of April, 1942, and the 30th day of April, 1942, and the said respondents-appellants appeal from each and every part of said order and from the whole thereof.

Also please take notice that said John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Co., Inc., Debtor, the above named respondents-appellants, on the above appeal will bring up for review:

(a) the above order entered in the office of the Clerk of the County of New York on March 27, 1942, overruling respondents-appellants objections to the jurisdiction of the Court,

(b) the above order entered in the office of the Clerk of the County of New York on April 30, 1942 denying respondents-appellants motion for resettlement of the order dated April 15, 1942; and

(c) so much of the order of the Appellate Division of the Supreme Court for the First Department entered in the office of the Clerk of said Court on the 19th day of [fol. 177] June, 1942, as affirms the aforesaid orders entered in the office of the Clerk of the County of New York on March 27, 1942, and April 30, 1942.

This appeal is taken as a matter of right, on the ground that there is directly involved the construction of the constitution of the United States.

Dated, New York, August 17, 1942.

Yours, etc., John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, One Wall Street, Borough of Manhattan, New York City, Respondents-Appellants Pro Se.

To: Satterlee & Warfield, 49 Wall Street, New York City. Greenbaum, Wolff & Ernst, 285 Madison Avenue, New York City, Attorneys for Petitioners-Respondents. George T. Campbell, Clerk of the above named Court.

[fol. 178] IN SUPREME COURT OF NEW YORK, APPELLATE DIVISION

ORDER OF AFFIRMANCE—June 19, 1942

Present: Hon. Francis Martin, Presiding Justice; Hon. Alfred H. Townley, Hon. Edward J. Glennon, Hon. Albert Cohn, Hon. Joseph M. Callahan, Justices.

12046, 12047, 12048

In the Matter of the Application of

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, J. FEARON BROWN, GEORGE KOEGLER and MURRAY MACELHINNY, individually and as co-partners doing business up to the close of business October 31, 1941 under the firm name and style of Kellogg, Emery & Inness-Brown and

LAWRENCE S. GREENBAUM, EDWARD S. GREENBAUM, HERBERT A. WOLFF, MORRIS L. ERNST, JONAS J. SHAPIRO, WALLACE D. JENNINGS, SAMUEL J. SCHUR and ALEXANDER LINDEY, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, Petitioners-Respondents,

for an order fixing the amount to which petitioners are entitled as compensation and for the determination and enforcement of their liens for services rendered in a certain action in this court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti, et al., Defendants; and a certain [fol. 179] action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward, Defendants, and a certain action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Company, Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendants

JOHN GERDES and JAMES D. CARPENTER, JR., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants

Appeals having been taken to this Court by John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds In-

vesting Company, Inc., Debtor, from an order of the Supreme Court, New York County, entered on the 27th day of March, 1942, overruling their objections to the jurisdiction of the court; from the final order of said court entered on the 15th day of April, 1942, adjudging that the petitioners have a lien to the extent of $102,250 upon the judgment entered in a certain cause of action in this court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti et al., Defendants; and adjudging that petitioners have a lien to the extent of $2,045 upon a cause of action in this court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodyard, Defendants; and adjudging that petitioners have a lien to the extent of $766.87 upon a cause of action in this Court entitled John Gerdes and James D. [fol. 180] Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendant; and from an order of said court entered on the 30th day of April, 1942, denying their motion to resettle the order entered on the 15th day of April, 1942.

And said appeals having been argued by Mr. John Gerdes of counsel for the appellants, and by Mr. Lawrence S. Greenbaum of counsel for the petitioners-respondents; and due deliberation having been had thereon,

It is hereby unanimously ordered that the said orders so appealed from be and the same are hereby affirmed, with costs and disbursements to the petitioners-respondents.

Enter,

E. J. G.

[fol. 181] AFFIDAVIT OF NO OPINION BY APPELLATE DIVISION

STATE OF NEW YORK,
County of New York, ss.:

Mary-Chase Clark, being duly sworn, says:

I am an attorney-at-law, associated with John Gerdes, one of the Trustees and attorneys pro se, one of the respondents-appellants in this proceeding and am familiar with all the proceedings herein.

No opinion was delivered by the Appellate Division, First Judicial Department.

Mary-Chase Clark.

Sworn to before me this 4th day of November, 1942. Christine Laverne, Notary Public, Nassau County. Certificate filed in New York County.

[fols. 182-183] IN SUPREME COURT OF NEW YORK, APPELLATE DIVISION

STIPULATION WAIVING CERTIFICATION OF RECORD TO COURT OF APPEALS—November 9, 1942

It is hereby stipulated and agreed by and between the attorneys for the respective parties hereto that the foregoing are true and correct copies of the Record on Appeal to the Appellate Division, First Department; the Order of Affirmance and the Notice of Appeal to the Court of Appeals, all of which are on file in the office of the Clerk of the County of New York.

Certification of all of the foregoing papers is hereby waived.

Dated, New York, November 4, 1942.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants, Pro se. Satterlee & Warfield and Greenbaum, Wolff & Ernst, Attorneys for Petitioners-Respondents.

[fol. 184] IN COURT OF APPEALS OF NEW YORK

[Title omitted]

SUPPLEMENTAL STATEMENT UNDER RULE 234

The respondents-appellants submit this supplemental record containing true copies of the order of this Court, dated December 10, 1942, granting permission to appeal from the final order of the Appellate Division, First Department, entered in the office of the Clerk of said Court on the 19th day of June, 1942, affirming the orders of the

Special Term of the Supreme Court, New York County, entered in the office of the Clerk of the County of New York on the 27th day of March, 1942, the 15th day of April, 1942, and the 30th day of April, 1942; and the notice of appeal dated December 16, 1942, served pursuant to the permission granted.

The original record on appeal from the order of affirmance as aforesaid was duly served and filed on the 16th day of November, 1942.

[fol. 185] IN SUPREME COURT OF NEW YORK, APPELLATE DIVISION

[Title omitted]

NOTICE OF APPEAL TO COURT OF APPEALS AFTER ENTRY OF ORDER ALLOWING APPEAL—December 16, 1942

[fol. 186] SIRS:

Please take notice that pursuant to leave granted by the Court of Appeals of the State of New York in the above entitled action, by an order duly made and filed in the office of the Clerk of that Court on the 10th day of December, 1942, John Gerdes and James D. Carpenter, Jr. as Trustees of Reynolds Investing Co. Inc., Debtor, the above named respondents-appellants, hereby appeal to the Court of Appeals from the final order of the Appellate Division of the Supreme Court for the First Department, entered in the office of the Clerk of said Court on the 19th day of June, 1942, affirming the orders of the Special Term of the Supreme Court, New York County, entered in the office of the Clerk of the County of New York on the 27th day of March, 1942, the 15th day of April, 1942, and the 30th day of April, 1942, and the said respondents-appellants appeal from each and every part of said order and from the whole thereof.

Also please take notice that said John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Co., Inc., Debtor, the above named respondents-appellants, on the above appeal will bring up for review:

(a) the above order entered in the office of the Clerk of the County of New York on March 27, 1942, overruling respondents-appellants objections to the jurisdiction of the Court,

(b) the above order entered in the office of the Clerk of the County of New York on April 30, 1942 denying respondents-appellants motion for resettlement of the order dated April 15, 1942; and

[fol. 187] (c) So much of the order of the Appellate Division of the Supreme Court for the First Department entered in the office of the Clerk of said Court on the 19th day of June, 1942, as affirms the aforesaid orders entered in the office of the Clerk of the County of New York on March 27, 1942, and April 30, 1942.

Dated, New York, December 16, 1942.

Yours, etc., John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, One Wall Street, Borough of Manhattan, New York City, Respondents-Appellants Pro Se.

To: Satterlee & Warfield, 49 Wall Street, New York City. Greenbaum, Wolff & Ernst, 285 Madison Avenue, New York City, Attorneys for Petitioners-Respondents. George T. Campbell, Clerk of the above named Court.

[fol. 188] In Court of Appeals of the State of New York

Present: Hon. Irving Lehman, Chief Judge, Presiding.

In the Matter of the Application of B. H. Inness Brown & others, individually and as co-partners doing business, &c., under the firm name and style of Kellogg, Emery & Inness-Brown and Lawrence S. Greenbaum and others, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, Petitioners-Respondents, for an order fixing the amount to which petitioners are entitled as compensation and for the determination and enforcement of their liens for services rendered in a certain action in this Court entitled: John Gerdes and another, Trustees of Reynolds Investing Co. Inc., Debtor, Plaintiffs, against Clarence K. Reynolds and others, Defendants; and a certain action in this Court entitled: John Gerdes and another, Trustees of Reynolds Investing Co. Inc., Debtor, Plaintiffs, against Clarence K. Reynolds and others, Defend-

ants, and a certain action in this Court entitled: John Gerdes and another, Trustees of Reynolds Investing Co. Inc., Debtor, Plaintiffs, against Globe Indemnity Co. Inc., Defendants. JOHN GERDES and another, as Trustees of Reynolds Investing Co., Inc., Debtor, Respondents-Appellants

ORDER ALLOWING APPEAL—December 10, 1942

[fol. 189] A motion for leave to appeal to the Court of Appeals in the above cause having been heretofore made upon the part of the respondents-appellants herein, and papers having been duly submitted thereon, and due deliberation thereupon had,

Ordered that the said motion be and the same hereby is granted.

John Ludden, Clerk. (Seal.)

A copy.

[fol. 189a] STIPULATION WAIVING CERTIFICATION OF RECORD TO COURT OF APPEALS—December 30, 1942

[Same title]

It is hereby stipulated and agreed by and between the attorneys for the respective parties hereto that the foregoing are true and correct copies of the Notice of Appeal to the Court of Appeals, which is on file in the office of the Clerk of the County of New York, and the order of the Court of Appeals granting leave to appeal which is on file with the Clerk of said Court.

Certification of all of the foregoing papers is hereby waived.

Dated, New York, December 30, 1942.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants, Pro Se. Satterlee & Warfield and Greenbaum, Wolff & Ernst, Attorneys for Petitioners-Respondents.

[fol. 190] IN THE COURT OF APPEALS OF NEW YORK

In the Matter of B. H. INNESS BROWN, et al., Individually and as Copartners under the Name of KELLOGG, EMERY and INNESS BROWN, et al., JOHN GERDES, et al., as Trustees of REYNOLDS INVESTING COMPANY, INC., Appellants.

Appeal on constitutional grounds from an order of the Appellate Division of the Supreme Court in the first judicial department, entered June 19, 1942, which unanimously affirmed (1) an order of the court at Special Term (Walter, J.), dated March 26, 1942, overruling objections of the appellants John Gerdes and James D. Carpenter, Jr., as trustees, to the jurisdiction of the court, (2) a further order of Special Term (Walter, J.), dated April 15, 1942, fixing the amounts of attorney's liens, and (3) an order of Special Term (Walter, J.), dated April 29, 1942, denying a motion by appellants to resettle the order dated April 15, 1942.

John Gerdes and *James D. Carpenter, Jr.*, for appellants.

John F. Davis, George Zolotar, W. Crosby Roper, Jr., and *David Ferber* for Securities and Exchange Commission in support of appellant's position.

David Paine, Lawrence S. Greenbaum, Theodore S. Jaffin and *James E. Dwyer* for respondents.

OPINION—April 22, 1943

FINCH, J.:

The question raised by this appeal is whether a State court may fix the fees of attorneys appointed by a Federal court subsequent to the filing of the reorganization petition of a debtor under chapter VIII (§ 77B) of the Bankruptcy Act (U. S. Code, tit. 11) to bring suit in a State court upon causes of action constituting assets of the estate of the debtor.

The controversy arose in the course of the administration of the assets of the Reynolds Investing Company, Inc., a debtor in proceedings then pending under the National Bankruptcy Act in the United States District Court for the District of New Jersey. The reorganization proceeding was commenced under chapter VIII (§ 77B) but was continued under chapter X after that chapter became effective. Petitioners-respondents, hereinafter called the attorneys, were appointed by the Federal court subsequent

to the filing of the reorganization petition, to render services in the administration of the estate under the National Bankruptcy Act. The services rendered were in the collection of claims, and were undertaken subject to the provisions of the Bankruptcy Act. The issue is whether the State court in which the suits were brought has jurisdiction to fix the fees of the attorneys in reducing the claim to judgment, or whether exclusive jurisdiction is in the Federal court in bankruptcy who appointed these attorneys and who alone can have adequate knowledge of the assets of the estate on the one hand, and on the other the total of costs, expenses and fees with the resultant proportionate percentage for cost of administration, and who alone is subject to the elaborate machinery established by the Congress in the Bankruptcy Act for the fixing of allowances.

[fol. 191] It is submitted that the Federal court in a reorganization proceeding has exclusive jurisdiction to award fees to attorneys appointed by it in payment of services to the bankrupt estate in the collection of claims in a State court. The Congress has power to make uniform laws upon the subject of bankruptcy. (U. S. Const., art. I, § 8, clause IV.) In the National Bankruptcy Act the Congress has set up a comprehensive system of bankruptcy administration and conferred exclusive jurisdiction upon the Federal courts. Chapter 10 of the Act (Bankruptcy Act, §§ 111, 114), under which this reorganization is proceeding expressly confers upon the United States District Court "exclusive jurisdiction of the debtor and its property wherever located." This is re-enforced by the specific provision that State courts shall have no jurisdiction over bankruptcy matters. (Federal Judicial Code, § 256; see, also, *Gross* v. *Irving Trust Co.*, 289 U. S. 342, *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478.). Not only does chapter 10 specifically confer exclusive jurisdiction of the debtor and its property upon the Federal court, but in addition there is specifically given exclusive jurisdiction to determine costs, expenses and reasonable compensation for services rendered in reorganization proceedings (Bankruptcy Act, §§ 62, 241-250), and there are set forth numerous meticulous provisions designed to make effective the control of the Federal court over fees and expenses. Allowances under chapter 10 may be made

only after a hearing upon notice to the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate (§ 247). No longer are allowances fixed in a hearing confined solely to the attorneys in interest, but under chapter 10 interested parties enjoy the statutory right to appear and be heard (§ 206 [U. S. Code, tit. 11, § 606]). In addition, attorneys seeking compensation must file a statement under oath showing whether they have acquired or transferred claims against or stock of the debtor after the commencement of the proceeding, and no compensation can be allowed to any attorney who, after assuming to act in that capacity, has purchased or sold claims or stock of the debtor (§ 249). Also an attorney seeking compensation must by affidavit inform the Federal court whether he has made any agreement with any person for a division of his compensation (§ 62). If allowances and fees could be awarded in the State courts, all these elaborate provisions for a notice and hearing to all the parties interested, and prohibition against attorneys dealing in claims against the estate of the debtor could be evaded, and fees in as many State courts as there were assets of the debtor which should be collected therein, would be fixed without regard to the amount of the total expenses and assets as a whole, since the State court is dealing only with particular claims and cannot have adequate knowledge of what will comprise the entire estate [fol. 192] as to assets and total costs, expenses and fees.

Also, since these attorneys were appointed by the court in this reorganization proceeding and nothing was said as to fees, the services of the attorneys were undertaken subject to all the provisions of the Bankruptcy Act with respect to the compensation for such services. Any attempted surrender of jurisdiction by the United States Court, even if that were possible, would have to be implied. This court has ruled that there may be no implied surrender of the jurisdiction of the Federal court over a matter arising in the course of a bankruptcy proceeding. (*Palmer* v. *Larchmont Manor Co.*, 284 N. Y. 288.) Under such circumstances, even if no exclusive jurisdiction had been given to the Federal court, the attorneys would in the normal course return to have their compensation fixed by the court by whom the appointment had been made. Where attorneys have been appointed in a reorganization

proceeding to deal with an asset belonging to the debtor, it is difficult to see how a provision of the New York Judiciary Law (§ 475) could constitutionally provide for a lien upon these assets. (*Kalb* v. *Feuerstein*, 308 U. S. 433, 439.)

The control provided by the Bankruptcy Act over costs and expenses of administration, particularly including fees and allowances, is an important part of the entire reorganization and bankruptcy system. The system aims to provide maximum protection and relief for embarrassed or insolvent debtors consistent with protection and fairness to creditors and security holders. If the system is to work with satisfaction, there must be a proper balance giving on the one hand fair remuneration to those who administer the system, and on the other hand a limitation upon the total cost of administration, so that the Act in operation does not become too expensive. Centralized control over expenses incident to reorganization in bankruptcy to supplant State and Federal equity procedures, so as to reduce the cost of corporate reorganization, was one of the forces making for the enactment of the reorganization and bankruptcy statutes. (*Callaghan* v. *Reconstruction Finance Corp.*, 297 U. S. 464.) The importance of this centralized control over expenses incident to reorganization is seen in the provision of the Act (§ 258 [U. S. Code, tit. 11, § 658]) providing that administration allowances for services rendered in State or Federal court proceedings, later supplanted by a reorganization proceeding, must be determined not in the court supervising the prior proceeding but in the reorganization court. (*Matter of Keystone Realty Holding Co.*, 117 F. (2d) 1003.)

The Bankruptcy Act and chapter 10 show congressional intent to treat a reorganization proceeding not as ordinary litigation between private parties, but as involving rights and interests of many members of the general public who are usually unrepresented or inadequately represented in the proceeding. As the Supreme Court of the United States has indicated, these statutory provisions are de-
[fol. 193] signed to facilitate the participation of these various interests in matters in which they have a vital concern, and in any event furnish so far as possible, safeguards for their protection. (*Securities & Exchange Commission* v. *U. S. Realty & Improvement Co.*, 310 U. S. 434.)

If we are correct in holding that the jurisdiction of the

Federal court to determine these fees is exclusive, then it would seem clear that no waiver by the Federal court under the circumstances in the case at bar has been attempted. It is unnecessary to consider whether it was within the power of the court to surrender this jurisdiction, since it would appear that both as a matter of law and as a matter of fact the retainer of these attorneys was subject to the condition that the amount of any fees would be fixed by the United States District Court. From first to last the trustees herein have insisted upon their claim that in the case at bar jurisdiction to make allowances to these attorneys did not reside in the State court but resided in the Federal court. The stipulation of July 9, 1941 not only did not constitute a surrender of jurisdiction by the United States District Court, but contained the following specific reservation: "7. Nothing herein shall constitute a waiver of the rights of petitioners or respondents to question the jurisdiction of the courts of the State of New York, or the United States District Court for the District of New Jersey, with respect to the determination of the existence, nature or extent of respondents' liens and the payment of their fees and disbursements in connection with the aforesaid litigation."

Respondents rely upon the cases of *Sherman* v. *Buckley* (119 F. 2d 280, cert. den., 314 U. S. 657) and *Cup Craft Paper Corp.* v. *Federal Paper Board Co.*, (262 App. Div. 91, appeal dismissed, 288 N. Y. 529). In both of these cases the attorneys were not appointed by the Bankruptcy Court, but were retained and their services were rendered to the bankrupts and the liens arose, before the bankruptcy. While it is true that in *Sherman* v. *Buckley* (*supra*) the attorney continued as an attorney of record after the bankruptcy, there is nothing in the record to show that any services were rendered by him after the bankruptcy and before the substitution of attorneys, and no claim was made by him for services after the initiation of the bankruptcy proceeding. In addition, the attorneys in both of these cases were discharged and not permitted to complete the services for which they had been employed under a single contract of contingent retainer, whereas the attorneys herein were permitted fully to perform the services for which they were appointed, namely to reduce the claims to judgment. Also in the *Sherman* and *Cup Craft* cases the claims for services were provable as debts of the bankrupt and were

not within the statutory provisions regulating allowances for services in the administration of a reorganization or bankruptcy estate. As already noted, in the case at bar the attorneys were appointed by the court pending the reorganization proceeding to perform services as agents and appointees of the court. The allowances for the attorneys were administration expenses covered by the allowance provisions of the Bankruptcy Act.

[fol. 194]

It follows that the orders appealed from should be reversed and the proceeding dismissed without costs. (See 290 N. Y. —.)

Rippey, Lewis and Desmond, JJ., concur; Lehman, Ch. J., Loughran and Conway, JJ., dissent (See *Sherman* v. *Buck log*, 119 F. 2d 280; certiorari denied, 314 U. S. 657).

Orders reversed, etc.

[fol. 195] In Court of Appeals of New York

State of New York, ss:

Pleas in the Court of Appeals, held at Court of Appeals Hall, in the City of Albany, on the 22nd day of April in the year of our Lord one thousand nine hundred and forty-three, before the Judges of said Court.

Witness, The Hon. Irving Lehman, Chief Judge, Presiding, John Ludden, Clerk.

Remittitur—April 22, 1943

In the Matter of the Application of B. H. Inness Brown, & ors. incl. and as co-partners doing business &c and ors. &c for an order fixing &c compensation &c, and enforcement of their lien &c John Gerdes and ano.,—Appellants. Lawrence S. Greenbaum & ors—Respondents.

Be It Remembered, That on the 7th day of November in the year of our Lord one thousand nine hundred and forty-two John Gerdes and ano., as Trustees of Reynolds Investing Company, Inc. the appellants in this cause, came here unto the Court of Appeals, in person and filed in the said Court a Notice of Appeal return and supplemental return thereto from the order of the Appellate Division of the Supreme Court in and for the First Judicial Depart

ment and Lawrence S. Greenbaum & ors. individually and as co-partners &c, the respondents in said cause, afterward appeared in said Court of Appeals by Satterlee & Warfield and others, their attorneys

Which said Notice of Appeal return and supplemental return thereto filed as aforesaid are hereunto annexed.

Whereupon, The said Court of Appeals having heard this cause argued by Messrs. John Gerdes and James D. Carpenter, Jr. appellants pro se and by Mr. David Paine, of counsel for the respondents brief filed by amicus curiae, and after due deliberation had thereon did order and adjudge that the orders herein be and the same hereby are reversed and proceeding dismissed without costs.

And it was also further ordered, that the records aforesaid, and the proceedings in this Court, be remitted to the said Supreme Court, there to be proceeded upon according to law.

Wherefore, it is considered that the said orders be reversed and proceeding dismissed without costs, as aforesaid. And hereupon, as well the Notice of Appeal, return and supplemental return thereto aforesaid as the judgment of the Court of Appeals aforesaid, by it given in the premises are by the said Court of Appeals remitted into the Supreme Court of the State of New York before the Justices thereof, according to the form of the statute in such case made and provided, to be enforced according to law, and which record now remains in the said Supreme Court, before the Justices thereof, etc.

John Ludden, Clerk of the Court of Appeals of the State of New York.

[fol. 196] Clerk's Certificate to foregoing document omitted in printing.

[fol. 197] In the Court of Appeals of New York

[Title omitted]

Order Denying Motion for Reargument—May 27, 1943

A Motion for a re-argument of the above cause, having been heretofore made upon the part of the petitioners-respondents herein, and papers having been duly submitted thereon, and due deliberation thereupon had:

Ordered, that the said motion be and the same hereby is denied with ten dollars costs and necessary printing disbursements.

A Copy.

Raymond J. Cannon, Deputy Clerk. (Seal.)

[fol. 198] In Supreme Court of New York, New York County

Present: Honorable Felix C. Benvenga, Justice.

In the Matter of the Application of

B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler and Murray MacElhinny, individually and as co-partners doing business up the close of business October 31, 1941, under the firm name and style of Kellogg, Emery & Inness-Brown and

Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners doing business under the firm name and style of Greenbaum, Wolff & Ernst, Petitioners-Respondents,

for an order fixing the amount to which petitioners are entitled as compensation and for the determination and enforcement of their liens for services rendered in a certain action in this court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Vincent E. Ferretti, et al., Defendants; and a certain action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Clarence K. Reynolds, Richard S. Reynolds and William F. Woodward, Defendants, and a certain action in this Court entitled John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor, Plaintiffs, against Globe Indemnity Co., Inc., Defendants.

John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, Respondents-Appellants.

ORDER ON REMITTITUR—June 4, 1943

The above named appellants having appealed to the Court of Appeals of the State of New York from an order [fol. 199] of the Appellate Division of the Supreme Court in and for the First Judicial Department, entered in the Office of the Clerk of said Court on June 19, 1942, affirming the orders of the Special Term of the Supreme Court, New York County, entered in the office of the Clerk of the County of New York, on the 27th day of March, 1942, the 15th day of April, 1942, and the 30th day of April, 1942, and the Court of Appeals having heard said appeal and having ordered and adjudged that the said orders be reversed and the proceeding dismissed without costs; and the above respondents having made a motion for a reargument of the said cause to the Court of Appeals of the State of New York and the Court of Appeals having after due deliberation thereon ordered that the said motion be denied with $10 costs and necessary printing disbursements, and the remittitur from the Court of Appeals having been filed herein.

Now, on motion of John Gerdes and James D. Carpenter, Jr., as Trustees of Reynolds Investing Company, Inc., Debtor, it is

Ordered, that the order and determination of the said Court of Appeals be, and the same hereby are, made the order and determination of this Court.

Further Ordered that this proceeding be dismissed without costs.

Enter.

F. C. B. J. S. C.

[fol. 200] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 201] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI. Filed October 11, 1943

The petition herein for a writ of certiorari to the Court of Appeals of the State of New York is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

FILE COPY

JUL 20 1943
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

October Term 1943

No. 183

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, J. FEARON BROWN, GEORGE KOEGLER, and MURRAY MACELHINNY, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

LAWRENCE S. GREENBAUM, EDWARD S. GREENBAUM, HERBERT A. WOLFF, MORRIS L. ERNST, JONAS J. SHAPIRO, WALLACE D. JENNINGS, SAMUEL J. SCHUR and ALEXANDER LINDEY, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

against

JOHN GERDES and JAMES D. CARPENTER, JR., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT, STATE AND COUNTY OF NEW YORK

DAVID PAINE,
LAWRENCE GREENBAUM,
Counsel for Petitioners.

Supreme Court of the United States

October Term 1943

No.

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, J. FEARON BROWN, GEORGE KOEGLER, and MURRAY MACELHINNY, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

LAWRENCE S. GREENBAUM, EDWARD S. GREENBAUM, HERBERT A. WOLFF, MORRIS L. ERNST, JONAS J. SHAPIRO, WALLACE D. JENNINGS, SAMUEL J. SCHUR and ALEXANDER LINDEY, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

against

JOHN GERDES and JAMES D. CARPENTER, JR., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT, STATE AND COUNTY OF NEW YORK *

To the Supreme Court of the United States:

The petitioners pray for a writ of certiorari to review a decision of the Court of Appeals of New York (290 N. Y. 468) which, in reversing, by a vote of four to three, the decision of the New York Supreme Court and the Appellate Division, determined that the New York Supreme Court was precluded from determining and enforcing the attor-

* The index and table of cases and statutes cited appear at the end hereof.

neys' lien of petitioners, as provided by Section 475 of the New York Judiciary Law (Consol. Laws, c. 30), because exclusive jurisdiction to fix petitioners' fees for services in plenary suits in the State Court in behalf of the debtor and Trustees, resided in the United States District Court, New Jersey, by virtue of the United States Constitution (Art. 1, § 8, Cl. IV) and the Bankruptcy Act (Chapter X).

Summary Statement of Matter Involved

Proceedings for the reorganization of Reynolds Investing Company, Inc. (referred to as Investing), under Section 77B of the Bankruptcy Act, were instituted on May 18, 1938 in the United States District Court of New Jersey (R. 11). On August 1, 1938, the Bankruptcy Court (Judge Fake) by specific order authorized Investing to commence an action in the Supreme Court of New York (referred to as the State Court) on certain claims in favor of Investing against its former officers, directors, and others, and to retain petitioners' law firms (referred to as the Attorneys) to prosecute the action (R. 12). On August 4, 1938, prior to the effective date of Chapter X of the Bankruptcy Act (Chandler Act), such an action was commenced in the State Court (R. 12).

On January 19, 1939, after the effective date of Chapter X, the Bankruptcy Court entered an order appointing respondents trustees of Investing (referred to as Trustees) and authorizing them to be substituted as parties plaintiff in and to continue the action which had been commenced pursuant to its order of August 1, 1938 (R. 12). The Trustees, upon their application, were duly substituted as parties plaintiff in the action by order of the State Court dated February 10, 1939 (R. 12).

Two other actions were commenced in 1940 by the Trustees in the State Court, with the petitioners as their Attorneys, pursuant to the authority of the Bankruptcy Court (R. 13, 16, 19).

The Attorneys brought the first action to trial and succeeded in obtaining an interlocutory judgment, holding the principal defendants liable to the Company and directing that they account to the Trustees in hearings before a Referee. The Attorneys conducted such hearings and final judgments were entered against various defendants, ranging in amount up to $1,310,109.13 (R. 13-15). No fee was ever paid them for services.

In June, 1941, while the petitioners were conducting the hearings before the Referee, and while the two other actions were pending undetermined (issue having been joined), the Trustees (who are members of the Bar) notified the Attorneys by letter that they were taking over all pending matters in the Attorneys' hands "except the conduct of the hearings before Referee Dunn"; that they were relieving the Attorneys "henceforth of the burden and responsibility of the litigation"; and that they themselves were going to handle pending appeals and the collection of the judgments in the first action (R. 20, 22). This notification was not based on any claim of neglect or wrongdoing on the part of the Attorneys, but solely on the absolute prerogative of a client to change his attorneys (R. 20).

Thereafter, upon refusal of the Attorneys to accede to the demand of the Trustees that they surrender papers and memoranda relating to the litigation unless their fees and disbursements were paid, the Trustees began a proceeding in the Bankruptcy Court to procure the same. The motion was resisted by the Attorneys. After argument in the Bankruptcy Court, the Trustees withdrew their motion pursuant to a stipulation, dated July 19, 1941, and signed "So Ordered" by the Judge of the Bankruptcy Court, which provided, among other things, that the Attorneys should institute proceedings in the State Court to fix their liens, with the reservation of rights to the Trustees to question the jurisdiction of that Court. It was stipulated and ordered that the Attorneys would "consent to the substitution of the Trustees or their attorneys" in place and stead of the Attorneys in all pending actions (R. 25).

Lien Proceedings in State Court

In accordance with the stipulation and order of the Bankruptcy Court, the Attorneys, in December, 1941, instituted a proceeding in the State Court to fix and enforce their liens in the three actions, pursuant to Section 475 (infra, pp. 5-6) of the Judiciary Law (R. 9-26). The Trustees interposed an answer contesting the jurisdiction of the New York Court to fix the liens, contending that exclusive jurisdiction over the State Court causes of action and the Attorneys' fees was vested in the Bankruptcy Court under the Constitution of the United States and the Bankruptcy Act; further, that the Attorneys had inferentially agreed with the Bankruptcy Court that their compensation and liens should be fixed by that Court (R. 26-67).

The State Court Justice entered an order overruling the Trustees' objections (R. 4-5) and wrote a comprehensive opinion on the entire subject (R. 98-109).

After the disposition of the jurisdictional issue, the State Court Justice conducted hearings upon the merits and entered a final order determining the reasonable value of the Attorneys' services (R. 6-8) in the three suits to be $102,750. This was based on over 9,000 hours of services, an extended trial, resulting in judgments for the Trustees of $1,310,000, and the use of plaintiffs' testimony by the Trustees in a similar action in Virginia (R. 15-6, 19, 111-3).

Proceedings in the Appellate Division

The Trustees appealed both the order overruling their jurisdictional objections and the order fixing the Attorneys' lien to the Appellate Division, First Department. That Court (all five Justices concurring) affirmed both orders without opinion, 264 App. Div. 852 (R. 118-9).

Proceedings in the Court of Appeals

By appeal as of right, upon the ground that the construction of the Constitution of the United States was directly involved (R. 116-7), and by permission granted, the Trustees appealed to the Court of Appeals (R. 121-2).

The Court of Appeals, by divided vote, reversed both orders and dismissed the proceedings (290 N. Y. 468), (R. 129-30), expressly noting in its statement of the nature of the appeal that it was an appeal on constitutional grounds (R. 124). Chief Judge Lehman and Judges Loughran and Conway dissented on the authority of *Sherman* v. *Buckley*, 119 F. (2d) 280, cert. den. 314 U. S. 657 (R. 129).

The Jurisdiction of This Court to Grant Certiorari

The jurisdiction of this Court is invoked under Judicial Code, Section 237(b), 28 USC Section 344(b).

The Court of Appeals, the highest Court of the State of New York, has dismissed the proceeding upon its construction of the Constitution of the United States and the Bankruptcy Act. According to such interpretation, exclusive jurisdiction is conferred upon the Bankruptcy Court which precludes the State Court from determining and enforcing the liens of the Attorneys under the New York Lien Law and confers an immunity to the debtor and its Trustees from the operation of such Lien Law. The New York statute thus involved, Section 475 Judiciary Law, Consol. Laws, c. 30, reads as follows:

> "§ 475. *Attorney's lien in action, special or other proceeding*
>
> "From the commencement of an action, special or other proceeding in any court or before any state or federal department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his

client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien. As amended L. 1936, c. 876; L. 1938, c. 34; eff. Sept. 1, 1938."

The Federal and constitutional questions and the claim of immunity were raised in the answer of the Trustees (R. 26-31) and passed upon by the Court of Appeals (R. 124-9).

This application is made within the three months allowed by 28 U. S. C. 350. The order of the Court of Appeals was made on April 22, 1943 (R. 129), reargument was denied on May 27, 1943 (R. 130); and on June 4, 1943, the order and determination of the Court of Appeals were made the order and determination of the Supreme Court, New York County (R. 131-2).

Constitution and Statutes Involved

The section of the Constitution of the United States and the Federal statutes involved will be found in the Appendix.

Questions Presented

1. Where a Debtor in Reorganization proceedings, pursuant to Chapter VIII (Sec. 77B) of the Bankruptcy Act retains attorneys and commences a plenary suit in a State Court, under specific order of the Reorganization Court, to enforce claims against third persons, and the Trustees of the Debtor, appointed under Chapter X of the Bankruptcy Act, are thereafter substituted as parties plaintiff in such action and prosecute it by the same attorneys, also under the specific order of the Reorganization Court, do

Article 1, Section 8, Clause IV of the Constitution of the United States, and the corporate reorganization provisions of the Bankruptcy Act preclude the State Court from determining and enforcing, under Section 475 of the Judiciary Law of New York State, the lien of such attorneys upon such cause of action, or the proceeds thereof, for their unpaid compensation for services in the action?

2. Where a Debtor in reorganization proceedings pursuant to Chapter VIII (Sec. 77B) of the Bankruptcy Act, and its Trustees, appointed later under Chapter X, retain attorneys and prosecute a plenary suit in a State Court under specific order of the Reorganization Court, to enforce claims against third persons, and the Trustees thereafter discharge the attorneys without cause before they have completed their services, and seek to substitute themselves pro se, or others as attorneys, does the State Court have jurisdiction to fix the lien of the discharged attorneys upon the causes of action in the State Court, and the proceeds thereof, as a condition of granting the substitution; or does the Constitution of the United States (Art. 1, Sec. 8, Cl. IV) and the Bankruptcy Act (Chaps. VIII and X) invest the Bankruptcy Court with exclusive jurisdiction to fix the attorneys' fees and preclude the State Court from proceeding under Section 475 of the Judiciary Law?

3. Where Trustees of a Debtor in Federal reorganization proceedings, under specific order of the Reorganization Court, commence or intervene in, and prosecute, plenary actions in a State Court upon choses in action in favor of the Debtor, do they thereby submit themselves to the jurisdiction of the State Court as to all incidents of the plenary action, including the determination of attorneys' liens thereon under Section 475 of the New York Judiciary Law?

4. Does a Reorganization Court, under Chapter VIII of the Bankruptcy Act (Sec. 77B), have jurisdiction as against

a State Court, of a cause of action in favor of the Debtor, which must be and is prosecuted by plenary suit in such State Court, together with the incidents of such suit, including the determination of the attorneys' lien?

5. Did the Reorganization Court, by virtue of the subsequent enactment of Chapter X, ever obtain jurisdiction over the causes of action which, with its consent, were commenced in the State Court when the Reorganization Court was proceeding under Chapter VIII (Sec. 77B)?

The Reasons for the Allowance of the Writ

1. In holding that the Bankruptcy Court had exclusive jurisdiction under the Constitution and the Bankruptcy Act, which precluded the Supreme Court, New York, from fixing the liens of the attorneys pursuant to Section 475, New York Judiciary Law, upon causes of action prosecuted in the latter Court on behalf of the Debtor and the Trustees under specific order of the Bankruptcy Court, the Court of Appeals has decided an important Federal question of substance not heretofore determined by this Court and in conflict with the decisions of the Circuit Court of Appeals for the Second (*Sherman* v. *Buckley*, 119 F. [2d] 280, cert. den. 314 U. S. 657) and Eighth Circuits (*Ohio Oil Company* v. *Thompson*, 120 F. [2d] 831, cert. den. 314 U. S. 658).

2. The Court of Appeals, in determining that the Federal Court did not surrender its jurisdiction to fix petitioners' fees, has determined a Federal question of substance in a way probably in conflict with the decisions of this Court. *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478; *Texas* v. *Donoghue*, 302 U. S. 284; *Foust* v. *Munson S.S. Lines*, 299 U. S. 77.

3. The Court of Appeals, in holding that the Bankruptcy Court had jurisdiction of the causes of action prosecuted

in the New York Supreme Court, has determined an important Federal question of substance in conflict with the decisions of the Circuit Court of Appeals and probably in conflict with the decisions of this Court. *In re Standard Gas & Elec.*, 119 F. (2d) 658, 663; *Tilton v. Model Taxi Corp.*, 112 F. (2d) 86, 88; *In re Prima*, 98 F. (2d) 952, 957, cert. den. *sub nom. Keig v. Harris Trust & Savings Bank*, 305 U. S. 658; *Taubel-Scott-Kitzmiller Co. v. Fox*, 264 U. S. 426; *Schumacher v. Beeler*, 293 U. S. 367.

Respondents and the Securities and Exchange Commission, which appeared as *amicus curiae* in the Court of Appeals, expressly stated that the appeal involved the construction of the reorganization provisions of the Bankruptcy Act and the respective jurisdictions of the Bankruptcy and State Courts and presented serious, novel and important questions in the administration of estates in reorganization under the National Bankruptcy Act which should be resolved by this Court.

WHEREFORE, your petitioners respectfully pray that this Petition for a Writ of Certiorari to the Supreme Court of the State of New York, New York County, be granted.

B. H. INNESS BROWN et al.,
Petitioners.

By DAVID PAINE,
LAWRENCE GREENBAUM,
Their Counsel.

Dated, July 19, 1943.

APPENDIX

CONSTITUTION AND FEDERAL STATUTES

Federal Constitution

ARTICLE I, SECTION 8, CLAUSE 4.

The Congress shall have Power To establish • • • and uniform laws on the subject of Bankruptcies throughout the United States;

Federal Statutes

JUDICIAL CODE, SECTION 256

(28 U. S. C. 371).

EXCLUSIVE JURISDICTION OF UNITED STATES COURTS.

The jurisdiction vested in the courts of the United States in the cases and proceedings hereinafter mentioned, shall be exclusive of the courts of the several States: • • •

Sixth. Of all matters and proceedings in bankruptcy.

Federal Bankruptcy Act

SEC. 23. JURISDICTION; UNITED STATES AND STATE COURTS.

a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the

bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67 and 70 of this Act.

SEC. 62. EXPENSES OF ADMINISTERING ESTATES; UNAUTHORIZED SHARING OF FEES; WITHHOLDING ALLOWANCES.—a. The actual and necessary costs and expenses incurred by officers in the administration of estates shall, except where other provisions are made for their payment, be reported in detail, under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred.

c. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, rendering services in a proceeding under this Act or in connection with such proceeding, shall not in any form or guise share or agree to share his compensation for such services with any person not contributing thereto, or share or agree to share in the compensation of any person rendering services in a proceeding under this Act, or in connection with such proceeding, to which services he has not contributed: *Provided, however,* That an attorney-at-law may share such compensation with a law partner or with a forwarding attorney-at-law, and may share in the compensation of a law partner.

d. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, seeking compensation for services rendered by him in a proceeding under this Act or in connection with such proceeding, shall file with the court his petition setting forth the value and extent of the services rendered, the amount requested and what allowances, if any, have theretofore been made to him. Such petition shall be accompanied by his affidavit stating whether an agreement or understanding exists between the petitioner and any other person for a division of compensation and, if so, the nature and particulars thereof. If

satisfied that the petitioner has, in any form or guise, shared or agreed to share his compensation or in the compensation of any other person contrary to the provisions of this subdivision, the court shall withhold all compensation from such petitioner.

SEC. 67. LIENS AND FRAUDULENT TRANSFERS.— * * *

b. The provisions of section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under chapters X, XI, XII, or XIII of this Act, by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

SEC. 111. EXCLUSIVE JURISDICTION OVER DEBTOR AND PROPERTY.

Where not inconsistent with the provisions of this chapter, the court in which a petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and its property, wherever located.

SEC. 114. MATTERS UPON APPROVAL OF PETITION; JURISDICTION, POWERS, AND DUTIES.

Upon the approval of a petition, the jurisdiction, powers, and duties of the court and of its officers, where not in-

consistent with the provisions of this chapter, shall be the same as in a bankruptcy proceeding upon adjudication.

SEC. 116. SAME; ADDITIONAL JURISDICTION OVER ADMINISTRATION OF ESTATE.

Upon the approval of a petition, the judge may, in addition to the jurisdiction, powers, and duties hereinabove and elsewhere in this chapter conferred and imposed upon him and the court—* * *

(2) authorize a receiver, trustee, or debtor in possession, upon such notice as the judge may prescribe and upon cause shown, to issue certificates of indebtedness for cash, property, or other consideration approved by the judge, upon such terms and conditions and with such security and priority in payment over existing obligations, secured or unsecured, as in the particular case may be equitable.

SEC. 148. ORDER OF APPROVAL AS STAY OF OTHER PROCEEDINGS.

Until otherwise ordered by the judge, an order approving a petition shall operate as a stay of a prior pending bankruptcy, mortgage foreclosure, or equity receivership proceeding, and of any act or other proceeding to enforce a lien against the debtor's property.

SEC. 206. PERSONS ENTITLED TO HEARINGS.

The debtor, the indenture trustees, and any creditor or stockholder of the debtor shall have the right to be heard on all matters arising in a proceeding under this chapter. * * *

SEC. 216. PROVISIONS OF PLAN.

A plan of reorganization under this chapter—* * *

(2) may deal with all or any part of the property of the debtor;

(3) shall provide for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge;

(10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein; the satisfaction or modification of liens, the cancellation or modification of indentures or of other similar instruments; the curing or waiver of defaults; the extension of maturity dates and changes in interest rates and other terms of outstanding securities; the amendment of the charter of the debtor; the issuance of securities of the debtor or such other corporations for cash, for property, in exchange for existing securities, in satisfaction of claims or stock or for other appropriate purposes;

(13) may include provisions for the settlement or adjustment of claims belonging to the debtor or to the estate; and shall provide, as to such claims not settled or adjusted in the plan, for their retention and enforcement by the trustee or, if the debtor has been continued in possession, by an examiner appointed for that purpose;

SEC. 221. CONFIRMATION BY COURT.

The judge shall confirm a plan if satisfied that—

(4) all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding

or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge;

SEC. 227. EXECUTION OF INSTRUMENTS, SATISFACTION OF LIENS, ETC.

The court may direct the debtor, its trustee, any mortgagees, indenture trustees, and other necessary parties to execute and deliver or to join in the execution and delivery of such instruments as may be requisite to effect a retention or transfer of property dealt with by a plan which has been confirmed, and to perform such other acts, including the satisfaction of liens, as the court may deem necessary for the consummation of the plan.

SEC. 241. PETITIONING CREDITORS; COURT OFFICERS; ATTORNEYS THEREFOR.

The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceedings under this chapter—

(3) by the trustee and other officers, and the attorneys for any of them;

(4) by the attorney for the debtor;

SEC. 242. REPRESENTATIVES AND OTHER PARTIES IN INTEREST; ATTORNEYS THEREFOR.

The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in connection with the administration of an estate in a proceeding under this chapter or in connection with a plan approved by the judge, whether or not accepted by creditors and stockholders or finally confirmed by the judge—

(1) by indenture trustees, depositaries, reorganization managers, and committees or representatives of creditors or stockholders;

(2) by any other parties in interest except the Securities and Exchange Commission; and

(3) by the attorneys or agents for any of the foregoing except the Securities and Exchange Commission.

SEC. 243. CREDITORS AND STOCKHOLDERS; ATTORNEYS THEREFOR.

The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred by creditors and stockholders, and the attorneys for any of them, in connection with the submission by them of suggestions for a plan or of proposals in the form of plans, or in connection with objections by them to the confirmation of a plan, or in connection with the administration of the estate. In fixing any such allowances, the judge shall give consideration only to the services which contributed to the plan confirmed or to the refusal of confirmation of a plan, or which were beneficial in the administration of the estate, and to the proper costs and expenses incidental thereto.

SEC. 244. PETITION FILED IN PENDING BANKRUPTCY PROCEEDING.

Where a petition is filed under section 127 of this Act, the judge may allow, if not already allowed, reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in the pending bankruptcy proceeding—

(1) by a marshal, receiver, or trustee, as provided in subdivision g of section 48 of this Act, and the attorneys for any of them;

(2) by the attorney for the petitioning creditors;

(3) by the attorney for the bankrupt; and

(4) by any other persons and the attorneys for any of them entitled under this Act to compensation or reimbursement in such bankruptcy proceeding.

SEC. 245. SAME; REFEREE IN BANKRUPTCY.

Where a petition is filed in a pending bankruptcy proceeding, the judge may allow reasonable compensation for services rendered and the proper costs and expenses incurred in such bankruptcy proceeding by a referee in bankruptcy. In fixing such compensation, the judge shall not be restricted by the provisions of section 40 of this Act.

SEC. 246. DISMISSAL OF PROCEEDING OR ADJUDICATION OF BANKRUPTCY.

Upon the dismissal of a proceeding under this chapter, or the entry of an order adjudging the debtor a bankrupt, the judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in such proceeding prior to such dismissal or order of adjudication by any persons entitled thereto, as provided in this chapter, and shall make provision for the payment thereof, and for the payment of all proper costs and expenses incurred by officers in such proceedings.

SEC. 247. HEARING OF APPLICATIONS.

The judge shall fix a time of hearing for the consideration of applications for allowances, of which hearing notice shall be given to the applicants, the trustee, the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate, * * *.

SEC. 248. DISMISSAL OF PROCEEDING AND REINSTATEMENT OF BANKRUPTCY; CHARGING OF ALLOWANCES IN BANKRUPTCY.

In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that a superseded bankruptcy be proceeded with, the compensation allowed by the judge, in the course of the proceeding under this chapter, to the referee, marshal, receiver, or trustee in the bankruptcy proceeding for services rendered by them in such bankruptcy proceeding shall be deemed to have been allowed in such bankruptcy proceeding, and such compensation shall be considered in connection with the making of future allowances therein or shall be readjusted, so as to comply with the provisions of this Act fixing their compensation in a bankruptcy proceeding.

SEC. 249. STATEMENT OF CLAIMS OR STOCK ACQUIRED OR TRANSFERRED AFTER COMMENCEMENT OF PROCEEDING.

Any person seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred.

SEC. 250. APPEALS.

Appeals may be taken in matters of law or fact from orders making or refusing to make allowances of compen-

sation or reimbursement, and may, in the manner and within the time provided for appeals by this Act, be taken to and allowed by the circuit court of appeals independently of other appeals in the proceeding, and shall be summarily heard upon the original papers.

SEC. 257. TRUSTEE OR DEBTOR IN POSSESSION VESTED WITH RIGHTS OF PRIOR FIDUCIARY.

The trustee appointed under this chapter, upon his qualification, or if a debtor is continued in possession, the debtor, shall become vested with the rights, if any, of such prior receiver or trustee in such property and with the right to the immediate possession thereof. The trustee or debtor in possession shall also have the right to immediate possession of all property of the debtor in the possession of a trustee under a trust deed or a mortgagee under a mortgage.

SEC. 258. PROTECTION OF OBLIGATIONS OF PRIOR FIDUCIARY; PAYMENT OF COSTS AND EXPENSES.

The judge shall make such provision as may be equitable for the protection of the obligations incurred by a receiver or trustee in such prior proceeding and for the payment of the reasonable costs and expenses incurred therein as may be allowed by the judge.

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FILED
JUL 20 1943
CHARLES ELMORE CROPLEY

Supreme Court of the United States

October Term 1943

No. 183

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, J. FEARON BROWN, GEORGE KOEGLER, and MURRAY MACELHINNY, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

LAWRENCE S. GREENBAUM, EDWARD S. GREENBAUM, HERBERT A. WOLFF, MORRIS L. ERNST, JONAS J. SHAPIRO, WALLACE D. JENNINGS, SAMUEL J. SCHUR and ALEXANDER LINDEY, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

against

JOHN GERDES and JAMES D. CARPENTER, JR., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

BRIEF IN SUPPORT OF PETITION

DAVID PAINE,
LAWRENCE GREENBAUM,
Counsel for Petitioners.

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Supreme Court of the United States

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No.

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, et al.,
Petitioners,

against

JOHN GERDES, et al.,
Respondents.

BRIEF IN SUPPORT OF PETITION

Opinions Below

The opinions of the Supreme Court are not officially reported, but appear at R. 98-113. The Appellate Division wrote no opinion; the opinion of the Court of Appeals and dissent therefrom are reported in 290 N. Y. 468 and appear at R. 124-9.

Jurisdiction

A statement as to jurisdiction appears in the petition, pages 5-6.

Statement of the Case

A summary statement of the facts is given in the petition, pages 2-5.

Statutes Involved

The constitutional provision and the statutes involved are set forth in an Appendix attached to the petition, except that Section 475 of the Judiciary Law of the State of New York is set forth in the petition, pages 5-6.

POINT I

The Court of Appeals has decided an important Federal question of substance not heretofore determined by this Court and in conflict with the decisions of the Circuit Court of Appeals for the Second and Eighth Circuits, in holding that the Bankruptcy Court had exclusive jurisdiction under the Constitution and the Bankruptcy Act, which precluded the State Court from fixing the liens of the Attorneys upon causes of action prosecuted in the State Court on behalf of the Debtor and the Trustees with the authority of the Bankruptcy Court.

Chief Judge Lehman and Judges Loughran and Conway dissented on the ground that the decision was in conflict with the ruling of the Circuit Court of Appeals for the Second Circuit in *Sherman* v. *Buckley*, 119 F. (2d) 280, cert. den. 314 U. S. 657.

An examination of the opinion, record and petition for certiorari in the *Sherman* case shows that the Court passed upon the very issue involved here and decided exactly contrary to the Court of Appeals.

The facts in the *Buckley* case follow:

Gould, by Buckley & Buckley, his attorneys, sued in the New York Supreme Court. The complaint was dismissed. In January, 1934, while an appeal was pending, Gould was adjudicated a bankrupt and Sherman was appointed trustee. The trustee then procured authorization of the Bankruptcy Court to proceed with the New York action in the name of Gould the bankrupt, the avails thereof, however, to inure to the bankrupt's estate. In 1935 the trustee determined to substitute other attorneys in place of the Buckley firm. Thereafter, upon motion by the trustee in the State Court, an order was entered substituting other attorneys for the

Buckley firm and fixing the latter's lien for services at 30% of any recovery obtained in the action. Subsequently, the case was settled for $40,000. The Buckley firm thereupon applied to the State Court for an order directing the defendants to pay them the amount of their lien. The trustee then applied to the Bankruptcy Court to enjoin the Buckley firm from enforcing their lien. He contended that the New York Court was "without jurisdiction to adjudicate the value of their lien"; that "the avails of the action belong to the Trustee in Bankruptcy and are within the custody of the United States District Court," and that the proceeding sought to be enjoined "constitutes an interference with the jurisdiction of that Court in its paramount right to administer the bankrupt estate" (Rec. on App., ff. 19-24, 31).

The District Court granted the injunction.

The Circuit Court of Appeals reversed and held that the District Court had no power to interfere with the Buckleys' lien or with their right to have it determined and enforced in the State Court. Rejecting the argument of the Trustee that the fixing of the lien constituted an interference with the exclusive bankruptcy jurisdiction of the Bankruptcy Court, the opinion (per L. Hand, J.) stated (p. 282):

> "• • • He [the trustee] could of course substitute other attorneys, as he did, and Buckley & Buckley were obliged to retire; but the substitution did not affect their charging lien under §475 of the Judiciary Law of New York, Consol. Laws, c. 30, or their possessory lien upon the papers.
>
> • • • • • • •
>
> "In spite of the fact that the jurisdiction of the bankruptcy court is usually described as 'exclusive,' it may consent to have the interests of third persons in property of which the bankrupt had possession, adjudicated in a state court if that is more convenient. *Foust* v. *Munson S. S. Lines*, 299 U. S. 77, 57 S. Ct. 90, 81 L. Ed. 49; *Texas* v. *Donoghue*, 302 U. S. 284,

58 S. Ct. 192, 82 L. Ed. 264; *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, 483, 60 S. Ct. 628, 84 L. Ed. 876; *In re Schulte-United, Inc.*, 2 Cir., 49 F. (2d) 264. As we have said, the trustee got the permission of the bankruptcy court to allow the action to be prosecuted in the state court. That necessarily involved a consent to such incidents as the exercise of that court's jurisdiction might involve, among them that, as a condition upon the substitution of new attorneys, the charging lien of the displaced attorneys must be liquidated."

Certiorari was denied (314 U. S. 657).

That the decision of the Circuit Court of Appeals in the *Sherman* case involved the identical issues presented here is plain from the petition for certiorari by the trustee in the *Sherman* case. There (Petition, pp. 30-31) the Trustees listed the questions involved as follows:

"The issues in the instant case raise several questions which are of the utmost importance, so that bankruptcy courts and their officers may know just what acts of theirs would constitute a consent that some other court determine questions which otherwise would rest solely in the jurisdiction of the bankruptcy court.

"These questions are as follows:

"1. Where a bankruptcy court consents that a trustee prosecute an action *in personam* in the name of a bankrupt, does such consent carry with it the implied consent that the court in which such action is pending may determine claims to or liens against the proceeds of such action?

"2. Where a trustee institutes, intervenes in, or continues in the name of a bankrupt, a plenary suit *in personam* for money damages, does the trustee thereby submit himself to the jurisdiction of the court in which such suit is instituted or is pending to the extent that such court may determine liens or claims, such as attorneys' liens, against the proceeds of such suit?

"3. Where a trustee, with the consent of the bankruptcy court, allows to be continued in the name of

> a bankrupt a plenary suit *in personam*, with the understanding that the fruits of such suit shall inure to the benefit of the bankrupt's estate, does he thereby submit himself to the jurisdiction of the court in which such suit is pending so that he is liable for costs, or attorneys' fees, etc.?"

The doctrine enunciated in *Sherman* v. *Buckley* was applied by the Circuit Court of Appeals (Second Circuit) in *New York Creditmen's Ass'n* v. *Schlesinger*, 126 F. (2d) 472. The Circuit Court of Appeals, Eighth Circuit, in *Ohio Oil Co.* v. *Thompson*, 120 F. (2d) 831, 836-837, cert. den. 314 U. S. 658, following the *Sherman* decision, has announced the same doctrine. Said Thomas, C. J., at pages 836-837:

> "• • • It has often been affirmed in cases of bankruptcy that, although the courts of the United States have exclusive jurisdiction 'of all matters and proceedings in bankruptcy', or, as stated in the opinion of the Supreme Court in this case, 'an exclusive and nondelegable control over the administration of an estate in its possession', when a trustee, having been given authority to do so, appears in a state court to litigate his right to property the state court has jurisdiction of all the incidents of the litigation, and its judgment in such action is binding upon him. (Citing Sherman v. Buckley and other cases.)"

These decisions are but an application of the rule that a trustee appointed under the Bankruptcy Act who becomes an active litigant in a State Court occupies the same status as any other litigant and is subject to such terms and conditions as the laws of the State impose upon the other litigants. *Boteler* v. *Ingels*, 308 U. S. 57; *In re Neely*, 113 Fed. 210 (C. C. A. 2); *Fischer* v. *Pauline Oil & Gas Co.*, 309 U. S. 294; *Ark. Corp. Commission* v. *Thompson*, 313 U. S. 132.

By Judiciary Law § 475, quoted above, the State of New York, to protect its attorneys, has imposed a condition upon persons seeking access to its courts, namely, that an

attorney under appropriate circumstances may have the New York Court determine and enforce his lien. The underlying principle of *Sherman* v. *Buckley* is that a trustee under the Bankruptcy Act is subject to this condition of local law just as he would be subject to other local laws or rules pertaining to litigation such as costs, execution, supplementary proceedings, etc. This principle was followed in *In re Prudence Co.*, 96 F. (2d) 157 (C. C. A. 2), cert. den. 305 U. S. 616, in which the Court, discussing the lien rights of a New York attorney who successfully prosecuted an action for the benefit of an estate in reorganization under Section 77B, stated (p. 160):

> "Success having been achieved, they [the trustees] can reap the benefit of the judgment, but they take it subject to the attorney's charging lien."

The decision of the Court of Appeals in the instant case works a complete nullification of lien laws so far as debtors and their trustees are concerned and clothes them with immunity from the operation of State laws not possessed by other litigants—a result inconsistent with that reached by the Circuit Court of Appeals and opposed to the recent statement in *Boteler* v. *Ingels*, 308 U. S. 57, 61, that "clearly, means of permitting such immunity from local laws will not be read into the Bankruptcy Act."

Thus, a sharp conflict exists between the Court of Appeals and the Circuit Courts of Appeal upon an important question of the construction of the reorganization statutes and their effect on the jurisdiction of State Courts. A definitive ruling is necessary to settle this conflict and to remove any doubt in the administration of estates under the reorganization provisions of the Bankruptcy Act and to define the scope and validity of attorneys' liens in actions instituted by debtors or their trustees in State Courts.

It is respectfully submitted that the present appeal furnishes an appropriate occasion for the granting of certiorari. See *Emil* v. *Hanley*, 130 F. (2d) 369, cert. granted

317 U. S. 621, aff'd U. S. , 87 L. Ed. 643; *Fidelity Assurance Corp.* v. *Sims*, 129 F. (2d) 442, cert. granted 317 U. S. 614, aff'd U. S. , 87 L. Ed. 725; *Gross* v. *Irving Trust Co.*, 61 F. (2d) 812, cert. granted 288 U. S. 598, aff'd 289 U. S. 342; *Palmer Clay Products Co.* v. *Brown*, 297 U. S. 227-228.

POINT II

The Court of Appeals in determining that the Federal Court did not surrender its jurisdiction to fix petitioners' fees has determined a Federal question in a way probably in conflict with decisions of this Court.

As noted, the plenary suits in the State Court were instituted under specific order of the Reorganization Court and were prosecuted therein with its approval.

In holding that this action of the Reorganization Court did not constitute a surrender of its jurisdiction and a submission of the debtor and its trustees to the State Court, the Court of Appeals decided the case in a way not only flatly at variance with *Sherman* v. *Buckley*, 119 F. (2d) 280 (C. C. A. 2nd), cert. den. 314 U. S. 657, and *New York Credit Men's Assn.* v. *Schlesinger*, 126 F. (2d) 472 (C. C. A. 2nd), but also probably in conflict with the decisions in this Court to the effect that when a Federal Court permits or authorizes its trustee to litigate claims in a State Court, it surrenders its jurisdiction over such claims and their incidents, and the trustee submits himself to and is bound by the laws of the State, statute or otherwise.

Foust v. *Munson S. S. Lines*, 299 U. S. 77;
State of Texas v. *Donoghue*, 302 U. S. 284;
Thompson v. *Magnolia Petroleum Co.*, 309 U. S. 478;
United States v. *Shaw*, 309 U. S. 495.

POINT III

In holding that a cause of action in favor of a debtor, which must be enforced in a State Court, is an asset within the jurisdiction of the reorganization court, the Court of Appeals has decided a Federal question of substance in conflict with decisions of Circuit Courts of Appeal, and, probably, in conflict with the decisions of this Court.

In the preceding argument, based upon *Sherman* v. *Buckley, supra,* it was assumed that the Bankruptcy Court initially had jurisdiction of the causes of action in favor of the debtor, and that by authorizing the institution of suit in the State Court it thereby surrendered its jurisdiction to that Court over the causes of action and the incidents thereof, including the attorneys' liens under local law.

The Court of Appeals is at odds with Circuit Courts of Appeals in holding that under the Bankruptcy Act in effect at the time the principal State suit was brought, the Bankruptcy Court had jurisdiction of the cause of action. The Federal rule is that jurisdiction at all times over such cause of action was in the State Court where suit had to be brought, so that it was only that part of the assets recovered in the State suit, less the amount of the attorneys' charging lien and other costs fixed by the State Court, that ever became subject to administration in bankruptcy.

Respondents urged below, and the Court of Appeals held, that under Chapter X of the Bankruptcy Act the jurisdiction of the Reorganization Court has been extended to embrace causes of action in favor of a debtor. Chapter X did not become effective until September 22, 1938. The petition for reorganization herein was filed May 18, 1938, and the principal New York action was brought on August 4, 1938.

In holding that Chapter X obtains, not Chapter VIII (Sec. 77B), the Court of Appeals is at variance with the Circuit Courts of Appeals, Second and Third Circuits.

Thus, in *In re Standard Gas & Elec. Co.*, 119 F. (2d) 658-663, where a company, in reorganization under Chapter VIII (Sec. 77B), commenced an action in the Federal Court against former officers in June, 1938, prior to the effective date of Chapter X, the Third Circuit held that the jurisdiction of the reorganization court was fixed by Section 77B. Maris, C. J., wrote:

> "The provisions of Chapter X are made applicable to reorganization proceedings but are not extended to plenary actions involving controversies at law or in equity, instituted before the effective date of that chapter."

Similarly, the Circuit Court of Appeals, Second Circuit, held in *Tilton* v. *Model Taxi Corp.*, 112 F. (2d) 86, 88 (per Patterson, C. J.):

> "In the Chandler Act (11 U. S. C. A., § 502) it is provided that section 23 of the Bankruptcy Act shall not be applicable to proceedings under Chapter X, and it may be that the District Court would have jurisdiction of an action of the present sort brought by a trustee appointed under that chapter, even where the defendant did not consent. The Chandler Act did not take effect until after joinder of issue in the present action, and we see no occasion to discuss whether the jurisdiction of the court has been broadened by the later legislation."

Indeed it would appear that an interpretation of Chapter X which would give it retroactive operation so as to impair or destroy the attorney's liens which had previously accrued under local law would render the statute as applied unconstitutional in depriving the attorney of property without due process of law.

Under the decisions of Circuit Courts of Appeals and of this Court, such jurisdiction under Section 77B did not

include causes of action in favor of a debtor in reorganization. *In re Prima Co.*, 98 F. (2d) 952, 957 (C. C. A. 7th), cert. den. *Keig* v. *Harris Trust & Savings Bank*, 305 U. S. 658; *In re Standard Gas & Elec. Co.*, 119 F. (2d) 658, 661-662 (C. C. A. 3d); *Tilton* v. *Model Taxi Corp.*, 112 F. (2d) 86 (C. C. A. 2d); *Taubel-Scott-Kitzmiller Co., Inc.* v. *Fox*, 264 U. S. 426.

The principal basis of these decisions rests upon the provisions of Section 23 of the Bankruptcy Act, which is in terms applicable to proceedings under Section 77B, but which is expressly inapplicable to proceedings under Chapter X.

In *Schumacher* v. *Beeler*, 293 U. S. 367, 374, this Court, examining the legislative history of Section 23, stated:

> "In enacting §23, it was clearly the intent of the Congress that the federal courts should not have the unrestricted jurisdiction of suits between trustees in bankruptcy and adverse claimants which these courts had exercised under the broad provisions of §2 of the Act of 1867."

Attention is particularly directed to the Court's opinion in *In re Standard Gas & Elec. Co., supra*, where Maris, J., said at pp. 661-2:

> "In a broad sense a claim by a debtor against a third person is property of the debtor. As such the reorganization court may direct its prosecution by the trustee of the debtor if it is appropriate to do so in order to effect the debtor's reorganization. But it is a species of property which may only be realized upon for the benefit of the debtor and its creditors by the successful prosecution of a plenary suit against the third persons involved. We have seen that section 77B does not purport to confer jurisdiction over those persons. Such claims must therefore be enforced by plenary suits brought in courts whose existing jurisdiction is appropriate to entertain them."

See also:

In re Prima Co., supra, per Spark, C. J., p. 957.

Not only did the Reorganization Court lack any jurisdiction to entertain causes of action in favor of the debtor, but, in addition, the State Court, in which the respondent Trustees were compelled to sue, had control of every phase and incident of the suit. Thus, it had power to cause the examination of third persons, determine whether the claim should be tried by court or jury, determine the amount owed the debtor by the third persons, approve settlement of the action, impose costs, issue execution and invoke proceedings supplementary to execution. Since such exclusive jurisdiction resides in the State Court with respect to causes of action owned by a debtor in reorganization, it seems strange to claim that the Reorganization Court had jurisdiction thereof. The New York Supreme Court (R. 107) logically said:

> "It is, indeed, a little short of an absolute contradiction to say that a bankruptcy court has possession of something which the trustee must go into another court in order to get."

On proper consideration of the Bankruptcy Act it would seem to follow conclusively that it is only that part of the cause of action which remained after the deduction of the attorneys' lien, and other costs and allowances imposed by the State Court, that ever became subject to administration in bankruptcy. This is in exact accord with the decision in *In re Prudence Co.*, 96 F. (2d) 157 (C. C. A. 2d), cert. den. 305 U. S. 616, discussed *supra*, p. 6.

Thus, with respect to the principal New York suit it is plain on two grounds, under the decisions referred to, that the lien upheld by the New York Court did not invade the exclusive jurisdiction of the Bankruptcy Court: First, this cause of action did not fall within the jurisdiction of the Bankruptcy Court; second, if it did, that Court surrendered

its jurisdiction to the State Court by directing the institution of suit there.

The other two actions were commenced after the effective date of Chapter X. They were, however, prosecuted by the Trustees in the State Court under specific order of the Bankruptcy Court. The liens allowed by Justice Walter in the Supreme Court covered these cases, as well as the main case. Assuming that Chapter X gave the Reorganization Court jurisdiction of those causes of action, that jurisdiction was surrendered to the State Court for the actions themselves and the incidents resulting. *Thompson* v. *Magnolia Company, Sherman* v. *Buckley, supra.*

In the present uncertain state of the law resulting from this decision of the Court of Appeals an extraordinary situation exists whereby, presumably, the State Court can exercise every control over the State Court litigations and its remedies and incidents, except the one right to fix the liens of attorneys therein under explicit local statute, and jurisdiction for that purpose would thus vest exclusively in the Reorganization Court. Of course, such divided control can lead only to confusion and was never heretofore contemplated by any court. It appears to be opposed to all other decisions on the question. The question is of importance and should be resolved by this Court.

Respectfully submitted,

DAVID PAINE,
LAWRENCE GREENBAUM,
Counsel for Petitioners.

Dated, July 19, 1943.

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CLERK

Supreme Court of the United States

OCTOBER TERM, 1943

No. [illegible]

[illegible] et al., etc.,

and

Lawrence S. [illegible], et al., etc.,

Petitioners,

against

Howe Gowen and James D. Carpenter, Jr., etc.,

Respondents.

PETITIONERS' REPLY BRIEF

DAVID PAINE,
LAWRENCE GREENBAUM,
Counsel for Petitioners.

Dated, September 8, 1943.

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Supreme Court of the United States

OCTOBER TERM 1943

No. 183

B. H. Inness Brown, et al., etc.,

and

Lawrence S. Greenbaum, et al., etc.,

Petitioners,

against

John Gerdes and James D. Carpenter, Jr., etc.,

Respondents.

PETITIONERS' REPLY BRIEF

It seems requisite to the Attorneys that a brief reply be submitted in view of various fallacious arguments and erroneous statements of fact contained in the Trustees' brief.

I

Alleged error in the record—the constitutional question.

The Trustees' assertion (Br., p. 8) that the opinion certified by the Court of Appeals is erroneous in stating that the appeal was upon constitutional grounds is utterly without foundation. By their own admission (Brief, p. 8) and as the record plainly shows (R. 117) they appealed on constitutional grounds, and this Court will not question the authenticity of the opinion so certified merely because in

the temporary Advance Sheets (not the final official reports) the State Reporter erroneously failed to state that the appeal was on constitutional grounds as well as by permission. Indeed, as will appear presently, the opinion of the Court of Appeals shows plainly that the constitutional and federal questions were the sole and decisive factors upon which the decision of that Court rests.

II

A federal question was presented and necessarily passed upon. The issue was not determined as a matter of local State law.

The Trustees' principal argument is that the State Court decided the issue upon a non-federal ground, namely, that in fact the Attorneys had agreed that their compensation would be fixed by the Reorganization Court and that such contract had not been abrogated by discharge of the Attorneys. The contention that such agreement was made was expressly rejected by both lower Courts whose findings with respect thereto were undisturbed by the Court of Appeals.

In their brief (p. 11) the Trustees quote certain language of the Court of Appeals to make it appear that the Court determined "as a matter of fact" that because the Attorneys approved the Plan of Reorganization their retainer was subject to the condition that their fees would be fixed by the Federal Court. The quoted portion of the opinion has no relation whatever to the claim that the Attorneys approved the Plan or participated as parties therein. The opinion of the Court of Appeals is silent upon this point. An examination of the Court's opinion will show that the quoted portion refers rather to the Court's construction of the provisions of the Bankruptcy Act which the Court found constituted, in the absence of an express agreement, an implied agreement that the fees of the

Attorneys would be fixed by the Federal Court. Obviously, the determination that certain provisions of the Bankruptcy Act must be deemed to constitute the terms of an implied contract between the Attorneys and the Trustees is not the determination of a question of local law but rather the determination of a federal question involving the construction of the Bankruptcy Act.

It is clear from the opinion of the Court that its decision rested solely upon the federal question. Thus, Judge Finch states the sole issue to be "whether the State Court * * * has jurisdiction * * * or whether exclusive jurisdiction is in the Federal Court * * *" (R. 125), and his conclusion that jurisdiction rests in the Federal Court is based wholly upon the argument that the Constitution and the National Bankruptcy Act place an exclusive and non-delegable jurisdiction in that Court. Only when Judge Finch has finished his argument in support of his conclusion does he refer to the relationship between the Attorneys and the Trustees, and then only by way of distinguishing the Federal cases which, the dissenting Judges of the Court of Appeals held, placed jurisdiction in the State Court. The consideration given to the federal question in the majority opinion and the dissent based upon *Sherman* v. *Buckley*, 119 F. (2d) 280, cert. den. 314 U. S. 657, contrasted with the incidental reference to the termination of the Attorneys' services is cogent evidence that the Court of Appeals was not disposing of the matter upon the question of local State law.

The Trustees, in order to distinguish the instant case from *Sherman* v. *Buckley, supra*, make the unwarranted statement (Trustees' Brief, pp. 6, 7) that there was "no substitution or application for substitution of attorneys or of the Trustees *pro se* * * *." The fact is that Justice Walter in his opinion (R. 99) found that there was an attempt by these two Trustees to substitute themselves in the lawsuits (both being attorneys) in place of the petitioners. Neither the Appellate Division, which affirmed without opinion, nor the Court of Appeals, which reversed on the opinion of Judge Finch, reversed this finding in any

respect. Judge Finch did not even mention the matter in his opinion. Concededly, the entry of judgment in the action terminated the services of the Attorneys as a result of the letter of June 3, 1941 (R. 22). After that date steps were taken on behalf of the Trustees by someone to bring about a settlement of the lawsuits. The Trustees say they did not act *pro se* and that no attorneys were substituted. It is hard to understand then how any settlement was effectuated or any judgments satisfied. Of course, the stipulation of July 9, 1941 (R. 24-6), embodied as an order by Judge Fake on July 10, 1941 (R. 26), specifically provides for a consent to substitution in these same suits (R. 25). As Judge Hand said in *Sherman* v. *Buckley, supra,* the State Court had the right "as a condition upon the substitution of new attorneys to require that the charging lien of the displaced attorneys must be liquidated" (p. 282). (See also, *Matter of Krooks,* 257 N. Y. 329; *Matter of Tillman,* 259 N. Y. 134; *Matter of Weitling,* 266 N. Y. 184.)

On page 12 of their brief the Trustees state "that the Attorneys conceded that if there were no wrongful discharge * * * the state court would have no jurisdiction * * *." This is misleading. There is no claim by the Attorneys that the discharge was "wrongful". The claim is that the discharge gave the Attorneys the immediate right to exercise the lien which was given them by Section 475 of the Judiciary Law and which existed from the time the actions were started. It is too well known to justify any question that a client can discharge his attorney at any time for good reason, or, as here, with no reason. Hence, there cannot very well be a "wrongful" discharge of an attorney (see *Matter of Krooks,* 257 N. Y. 329, 331).

The suggestion contained in the Trustees' argument that the lien is extinguished upon the entry of judgment, thus permitting unconscionable clients to appropriate the fruits of the attorneys' labors, is contradicted by the history of attorneys' liens and the decided cases in New York. As Justice Walter stated (R. 100), the charging lien of an attorney at common law "did not arise until judgment was

recovered, whereas under the statute which is now section 475 of the Judiciary Law it exists upon the cause of action from the commencement of the suit or proceeding for the enforcement thereof." Certainly it was not the intention of the Legislature to abolish the lien, which the common law gave, once a judgment had been entered, but rather to enlarge the attorneys' rights by making the lien effective from the commencement of the action. Yet this would be the effect if the construction sought by the Trustees is sound.

III.

The federal question is not moot.

Except for one point, the argument advanced in Point II of the Trustees' brief has been completely answered in petitioners' main brief (see Main Brief, Points I and II). The single exception is the argument that the federal question of jurisdiction is moot because the Attorneys are bound by the Plan of Reorganization and the order confirming it, which provides that the Federal Court shall fix fees. This argument is based upon the wholly unfounded statement that "The attorneys were parties to the reorganization proceeding" (Trustees' Brief, p. 15). This misleading inference is drawn from the fact that as attorneys for security holders in the reorganization proceedings petitioners, on behalf of their clients, approved the Reorganization Plan. They were not parties at all. They were retained to bring suit almost two years before the Plan was confirmed (R. 31). Their lien attached upon the commencement of the suit (see Sec. 475, Jud. Law; Petitioners' Brief, pp. 5, 6).

It is perhaps sufficient to note that the Trustees have made no attempt by citation to the record to support their erroneous statement that petitioners were parties to the Plan, but the conclusive answer to that argument is that the Court of Appeals failed to adopt it, and since the Court

made no mention thereof, presumably it rejected it and affirmed the findings of the lower Courts (R. 108, 118-19) to the effect that the attorneys were not bound by the Plan of Reorganization, that the Plan was not *res judicata* upon the question of the Attorneys' fees, and that the Attorneys did not agree to waive their liens accorded to them under Section 475 of the Judiciary Law.

On page 3, in paragraph 3, and at the bottom of the page, and also on page 16, the Trustees seek to have the Court infer that the Attorneys by enforcing their lien have "attacked collaterally" the Plan of Reorganization. No attack has been made on that Plan collaterally or in any other way. The lien of these Attorneys arose outside the scope of that Plan and long prior to the submission of the Plan. It is quite independent of the Plan and its enforcement in no respect infringes upon the Plan.

CONCLUSION

The question here is one of importance. It involves the construction of the Bankruptcy Act and of the United States Constitution. It should be passed upon finally by this Court. The New York Court of Appeals by a bare majority has come to a conclusion quite contrary to that of several of the Circuit Courts of Appeals and apparently to the United States Supreme Court.

The writ should be allowed.

Respectfully submitted,

DAVID PAINE,
LAWRENCE GREENBAUM,
Counsel for Petitioners.

Dated, September 8, 1943.

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CLERK

Supreme Court of the United States

OCTOBER TERM, 1943

No. 183

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, et al.,

Petitioners,

vs.

JOHN GERDES and JAMES D. CARPENTER, JR., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW YORK.

PETITIONERS' BRIEF

DAVID PAINE,
LAWRENCE S. GREENBAUM,
WILLIAM C. SCOTT,
Solicitors for Petitioners.

THEODORE S. JAFFIN,
JAMES F. DWYER,
of Counsel.

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Supreme Court of the United States

OCTOBER TERM, 1943

No. 183

B. H. Inness Brown, David Paine, Ethelbert Warfield, et al.,

Petitioners,

vs.

John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW YORK.

PETITIONERS' BRIEF

Statement

The case is here on certiorari to review a decision of the New York Court of Appeals which determined, by vote of 4 to 3, that the New York Supreme Court was precluded from fixing and enforcing the attorneys' liens claimed by petitioners herein under Section 475 of the New York Judiciary Law, upon causes of action prosecuted in the State Court on behalf of the Debtor in reorganization and its Trustees with the authorization of the Bankruptcy Court. The basis of the decision, which reversed a contrary ruling by a unanimous Appellate Division affirming Special

Term of the Supreme Court and dismissed the lien proceeding for lack of jurisdiction, was that exclusive jurisdiction to fix fees for petitioners' services was vested in the Bankruptcy Court by virtue of the Constitution of the United States (Art. 1, § 8, Cl. IV) and the Bankruptcy Act (Chap. X).

Opinions Below

The Special Term of the Supreme Court (Justice WALTER), wrote opinions which are not officially reported but appear at pages 98 to 109 of the Record. The Appellate Division affirmed without opinion, such affirmance being reported in 264 N. Y. App. Div. 852 (R. 118-119). The opinion of the Court of Appeals is reported in 290 N. Y. 468 (R. 124-129). The three dissenting Judges (LEHMAN, C.J., LOUGHRAN and CONWAY, JJ.) relied upon *Sherman* v. *Buckley*, 119 F. (2d) 280, *cert. den.* 314 U. S. 657. 290 N. Y. 476 (R. 129).

Grounds of Jurisdiction

Certiorari was applied for under Section 237(b) of the Judicial Code (28 U. S. C., § 344[b]) and was granted by this Court on October 11, 1943 (R. 133). A federal question is involved.

Statement of the Case*

Proceedings for the reorganization of Reynolds Investing Co., Inc. (referred to as the Debtor) under Section 77B of the Bankruptcy Act were instituted on May 18, 1938 in the United States District Court of New Jersey (R. 11, 98). On August 1, 1938, some months prior to the approval of the petition, the Bankruptcy Court (Judge FAKE) by

* A chronology is contained in Appendix A, pp. 1 to 3, separately bound.

specific order authorized the Debtor to commence an action in the Supreme Court of New York (referred to as the State Court) to enforce and collect certain claims in favor of the Debtor against its former officers and others, based upon breaches of trust and conversion of company assets, and to retain petitioners herein (referred to as the Attorneys) to prosecute the action (R. 12, 98, 125). On August 4, 1938, prior to the effective date of Chapter X of the Bankruptcy Act (i.e., Sept. 22, 1938), such action (referred to as Action No. 1) was commenced in the State Court in accordance with the order of the Bankruptcy Court (R. 12, 98).

In this action and two others presently to be discussed the liens in question arose.

On January 19, 1939, subsequent to the effective date of Chapter X, the Bankruptcy Court after hearings held before it entered an order approving the petition for reorganization and appointing John Gerdes and James D. Carpenter, Jr., respondents here, as Trustees of the Debtor (referred to as the Trustees). The order authorized the Trustees to be substituted as parties plaintiff and to continue Action No. 1 (R. 12, 98). The Trustees, upon their own application, were duly substituted as parties plaintiff in the action by order of the State Court dated February 10, 1939 (R. 12, 98).

Two other actions were commenced in 1940 in the State Court by the Trustees with the Attorneys representing them under the order of the Bankruptcy Court (R. 13, 16-19, 98); one against the former directors of the Debtor based upon other breaches of trust (referred to as Action No. 2); the other against Globe Indemnity Co. upon fiduciary bonds covering the corporate officers (referred to as the Globe Action). Action No. 1 is the principal action; the other two are of comparatively minor importance so far as the extent of the Attorneys' services is concerned.

After extensive preparation, the Attorneys brought Action No. 1 to trial in January, 1941 before Mr. Justice

WALTER of the Supreme Court, New York County. The trial consumed six weeks, and at the conclusion thereof the Attorneys were successful in obtaining an interlocutory judgment dated April 24, 1941 holding the principal defendants liable to the Debtor and directing that they account to the Trustees in hearings before a referee, Mr. Dunn* (R. 14-15, 98). The Attorneys conducted such hearings; thereafter the Referee filed a report which was confirmed, and final judgments were entered on November 5, 1941. The judgments were obtained against ten defendants, ranging in amounts up to $1,310,109.13 (R. 15).

On June 3, 1941, while the Attorneys were conducting the hearings before the Referee in Action No. 1, the Trustees (who are members of the bar) notified the Attorneys by letter that they were taking over all pending matters in the Attorneys' hands "except the conduct of the hearings before Referee Dunn"; that they were relieving the Attorneys "henceforth of the burden and responsibility of the litigation"; that "this applies as well to the second cause of action now pending" (Action No. 2); and that they themselves were going to handle pending appeals and the collection of the judgments in the first action (R. 20, 22-23, 98-99). This notification was given five months before final judgment was entered in Action No. 1 and while the other two actions were pending untried, issue having been joined.† It was not based upon any claim

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* The decision of the Court is reported in 28 N. Y. Supp. (2d) 622-667.

† The Trustees in their brief in opposition to the petition for certiorari departed from the Record and stated that the Globe Action was abandoned and that neither the Attorneys nor the Trustees believe that there is a reasonable prospect of recovery. They further stated that Action No. 2 was settled. These statements are incorrect. The Globe Action was never abandoned; issue was joined and no steps whatever taken to withdraw or discontinue it. Action No. 2 was pending and at issue at the time the Attorneys were relieved of their duties, and the settlement referred to took place months later.

As Justice WALTER found: "The other two actions have not yet been tried and are still pending undetermined" (R. 98).

of neglect or wrongdoing on the part of the Attorneys, but solely upon the absolute prerogative of a client to change his attorneys (R. 20, 99).

In their notification of June 3, 1941 the Trustees requested the Attorneys to make available papers and memoranda relating to the litigation. By letter dated June 4, 1941 the Attorneys advised the Trustees that they would accede to such request when their fees and disbursements were paid (R. 23-24, 99).

On June 20, 1941 the Trustees commenced a proceeding in the Bankruptcy Court before Judge FAKE to direct the Attorneys to turn over their papers and memoranda. The motion was resisted by the Attorneys on the ground that the actions having been commenced in the State Court with the authority of the Bankruptcy Court, all incidents in connection with such actions, including the nature and extent of their possessory and charging liens and the enforcement thereof in accordance with the New York Lien Laws, were vested exclusively in the State Court (R. 20, 99). After argument in the Bankruptcy Court the Trustees withdrew their motion pursuant to a stipulation dated July 9, 1941 and signed "SO ORDERED" by Judge FAKE. This stipulation and order provided among other things (R. 24-26, 99) that the Attorneys would "commence proceedings in the state courts of New York for the fixation of their said liens, if any" and "will consent to the substitution" of the Trustees or other attorneys in the pending actions; that the stipulation and order did not constitute a waiver by the Attorneys "of their attorneys' liens, if any, or any other rights which they may possess, under the laws of the State of New York, and all such rights are hereby reserved"; and that the Trustees reserved the right to challenge the jurisdiction of the State Court.

The Trustees' letter of June 3, 1941, and the stipulation and order of July 9, 1941, are of importance in view of the position taken by the Trustees that the Attorneys were not discharged.

Proceedings Below

Lien Proceeding in State Court

In accordance with the stipulation and order of the Bankruptcy Court, the Attorneys in December, 1941 instituted a proceeding in the State Court to fix and enforce their liens on the three actions pursuant to Section 475 of the Judiciary Law (R. 9-26). To avoid misconception it is essential to point out that the services for which the Attorneys sought to impress liens related solely and exclusively to services performed by them in the State Court in prosecuting the actions (R. 16, 19, 21). No fees of any nature have ever been received for such services.

The Trustees interposed an answer to the petition in the State Court objecting to the jurisdiction of that Court to fix the liens, contending that exclusive jurisdiction over the State Court causes of action and the Attorneys' fees was vested in the Bankruptcy Court under the Constitution of the United States and the Bankruptcy Act; further, that the Attorneys had agreed inferentially with the Bankruptcy Court that their compensation should be fixed by that Court (R. 26-27). The Attorneys interposed a reply containing an absolute denial of any such agreement (R. 68). The State Court entered an order (R. 4-5) overruling the Trustees' jurisdictional objection and wrote a comprehensive opinion on the subject which, among other things, negatived the existence of any such agreement as alleged by the Trustees (R. 98-109).

After the disposition of the jurisdictional issue the State Court conducted hearings upon the merits and entered a final order fixing the value of the Attorneys' services in Action No. 1 at $100,000; in Action No. 2 at $2,000 and in the Globe Action at $750; and fixed liens upon the causes of action for the foregoing respective amounts (R. 6-8). The award in Action No. 1 was based upon upwards of 8,800 hours of services and an extended trial resulting in

substantial judgments for the Trustees. Another important factor which the Court took into consideration was the availability through stipulation of the voluminous record in Action No. 1 for use by the Trustees in a similar pending action instituted by them in Virginia against other defendants over whom jurisdiction could not be obtained in New York (R. 15-16, 19, 111-113).

Proceedings in the Appellate Division

The Trustees appealed from the order overruling their jurisdictional objection and the order fixing the Attorneys' liens. The Appellate Division, First Department, all five justices concurring, affirmed the orders without opinion (264 N. Y. App. Div. 852) (R. 118-119).

Proceedings in the Court of Appeals

As of right, upon the ground that the construction of the Constitution was directly involved (R. 116-117), and by permission granted, the Trustees appealed to the Court of Appeals (R. 121-122).

That Court by vote of 4 to 3 reversed both orders and dismissed the proceedings (290 N. Y. 468) (R. 129-130), expressly noting in its statement of the nature of the appeal that it was an appeal on constitutional grounds (R. 124). Motion for reargument was denied by the Court of Appeals on May 27, 1943 (290 N. Y. Mem., p. 324) (R. 130-131).

Specification of Error

The Court of Appeals erred in holding that the Supreme Court of New York did not have jurisdiction to fix the liens of the Attorneys under the New York Judiciary Law, Section 475, upon the causes of action prosecuted in the State Court under the specific and unqualified order of the Bankruptcy Court.

Constitution and Statutes Involved

Federal Constitution

Article I, § 8, Cl. 4

"The Congress shall have power to establish • • • uniform laws on the subject of Bankruptcies throughout the United States."

Federal Statutes

The provisions of Section 256 of the Judicial Code and sections of the Federal Bankruptcy Act will be found in Appendix B, pages 4 to 13 (separately bound).

New York Lien Law

Section 475 of the New York Judiciary Law (Consol. Laws, Chap. 30) reads as follows:

> "§ 475. *Attorney's lien in action, special or other proceeding.*
>
> "From the commencement of an action, special or other proceeding in any court or before any state or federal department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien."

Questions Presented

1. Where a Debtor in Reorganization proceedings pursuant to Chapter VIII (Sec. 77B) of the Bankruptcy Act, retains attorneys and commences a plenary suit in a State Court, under specific order of the Bankruptcy Court, to enforce claims against third persons, and the Trustees of the Debtor, appointed under Chapter X of the Bankruptcy Act, are thereafter substituted as parties plaintiff in such action and prosecute it by the same attorneys, also under the specific order of the Bankruptcy Court, do Article 1, Section 8, Clause IV of the Constitution of the United States, and the corporate reorganization provisions of the Bankruptcy Act preclude the State Court from determining and enforcing, under Section 475 of the Judiciary Law of New York State, the lien of such attorneys upon such cause of action, or the proceeds thereof, for their unpaid compensation for services in the action?

2. Where a Debtor in reorganization proceedings pursuant to Chapter VIII (Sec. 77B) of the Bankruptcy Act, and its Trustees, appointed later under Chapter X, retain attorneys and prosecute a plenary suit in a State Court under specific order of the Bankruptcy Court, to enforce claims against third persons, and the Trustees thereafter discharge the attorneys without cause before they have completed their services, and seek to substitute themselves pro se, or others as attorneys, does the State Court have jurisdiction to fix the lien of the discharged attorneys upon the causes of action in the State Court, and the proceeds thereof, as a condition of granting the substitution; or does the Constitution of the United States (Art. 1, § 8, Cl. IV) and the Bankruptcy Act (Chaps. VIII and X) vest in the Bankruptcy Court exclusive jurisdiction to fix the attorneys' fees and preclude the State Court from proceeding under Section 475 of the New York Judiciary Law?

3. Where Trustees of a Debtor in Federal reorganization proceedings, under specific order of the Bankruptcy Court, commence or intervene in, and prosecute, plenary actions in a State Court upon choses in action in favor of the Debtor, do they thereby submit themselves to the jurisdiction of the State Court as to all incidents of such actions, including the determination of attorneys' liens thereon under Section 475 of the New York Judiciary Law?

4. Does a Bankruptcy Court, under Chapter VIII of the Bankruptcy Act (Sec. 77B), have jurisdiction as against a State Court, of a cause of action in favor of the Debtor, which must be and is prosecuted by plenary suit in such State Court, together with the incidents of such suit, including the determination of the attorneys' lien?

5. Did the Bankruptcy Court, by virtue of the subsequent enactment of Chapter X, ever obtain jurisdiction over the causes of action which, under its order, were commenced in the State Court while the Bankruptcy Court was proceeding under Chapter VIII (Sec. 77B)?

Summary of Argument

1. The State Court had jurisdiction to fix the Attorneys' liens upon the causes of action on the following grounds:

(a) The causes of action upon which the liens were fixed were prosecuted by the Debtor and its Trustees by the express and unqualified order of the Bankruptcy Court. This constituted a submission to the jurisdiction of the State Court respecting all incidents of the litigation including the determination and enforcement of the Attorneys' liens (Point I, p 11, *infra*).

(b) The Trustees, by seeking a substitution of themselves as attorneys in the State Court, subjected themselves to such conditions as that court might impose, including

the liquidation of liens of the Attorneys (Point II, p. 23, *infra*).

2. Under Section 77B, which was in effect when Action No. 1 was instituted, jurisdiction over such action and its incidents was never in the Bankruptcy Court, but became vested exclusively in the State Court (Point III, p. 26, *infra*).

3. Neither Section 77B nor Chapter X prohibited the State Court from fixing liens upon causes of action prosecuted in that Court with the authorization of the Bankruptcy Court (Point IV, p. 36, *infra*).

4. The determination and enforcement of the liens by the State Court is not inconsistent with any alleged contract or agreement made by the Attorneys with the Trustees or the Bankruptcy Court (Point V, p. 45, *infra*).

POINT I

The prosecution by the Debtor and the Trustees of the suits in the State Court with the express and unqualified authorization of the Bankruptcy Court conferred jurisdiction upon the State Court to determine and enforce the Attorneys' liens upon such suits pursuant to the New York Lien Law.

Assuming for the purposes of this Point that the Bankruptcy Court originally had jurisdiction of the causes of action in favor of the Debtor and the Trustees, Justice WALTER supported the jurisdiction of the State Court to fix and enforce the liens upon the following principal ground, among others:

> "I am of the opinion that the short, simple, conclusive and all sufficient answer to the contention of the trustees is that first the bankrupt and then they them-

selves, both with the approval and by direction of the bankruptcy court, voluntarily became active litigants in this court with petitioners as their attorneys, and they thereby submitted themselves to the jurisdiction of this court respecting all incidents of that litigation * * *. Asserting a claim in a court is a waiver of immunity from its process at least as to that claim and its incidents [Citing cases]" (R. 99).

After analyzing the provisions of the Bankruptcy Act and the relevant decisions* he concluded (R. 108):

"The bankruptcy court thus may and sometimes should permit state courts to determine rights and questions affecting property which is either actually or constructively in its possession, and where, as here, the bankruptcy court has authorized the institution of actions in this court, and the trustees have become litigants in this court through attorneys authorized by them and by the bankruptcy court, there can be no doubt of the jurisdiction of this court to carry the litigation through to its end, including the incident of fixing and enforcing the attorney's lien (*Sherman* v. *Buckley*, 119 Fed. 2d, 280 [*cert. den.* 314 U. S. 657]: *Ohio Oil Co.* v. *Thompson*, 120 Fed. 2d, 831, 836, second column [*cert. den.* 314 U. S. 658]). Choice was made when the trustees became parties to the litigation in this court. They cannot revoke that choice now."

This decision is sound in its reasoning and is supported by the authorities, as will presently appear.

A. By virtue of the New York Attorneys' Lien Law, litigation handled by New York attorneys is charged with a lien in their favor.

Section 475 of the Judiciary Law provides:

"From the commencement of an action * * * in any court * * * the attorney who appears for a party has

* Including, among others, *Foust* v. *Munson S. S. Lines*, 299 U. S. 77, 86 (1936); *State of Texas* v. *Donoghue*, 302 U. S. 284 (1937); *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478 (1940), discussed *infra*.

> a lien upon his client's cause of action * * * which attaches to a verdict * * * judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come * * *."

And that

> "The court upon the petition of the client or attorney may determine and enforce the lien."

By this section the State of New York, in order to protect its attorneys, has placed a condition upon the right of litigants who seek access to a court in the State by granting a charging lien to the attorney upon the client's cause of action, the judgment and proceeds thereof. Thus, at the threshold of his relationship with a New York attorney a litigant is put on notice that from that time forward his claim or cause of action is burdened with a lien subject to determination by a tribunal located in New York.

The nature, extent and enforcement of such charging lien under the foregoing section of the Judiciary Law (which is similar to provisions in other States) have been clearly defined by the New York courts. Briefly summarized:

1. The lien is a right granted to the attorney to have the proceeds of his client's cause of action applied to the payment of his charges for services rendered in connection with the action.. *Goodrich* v. *McDonald*, 112 N. Y. 157, 162-165 (1889); *Matter of Heinsheimer*, 214 N. Y. 361 (1915).

2. It is a substantive right,—the attorney being regarded as in the position of an "equitable assignee" of the client's cause of action *pro tanto*. *Beecher* v. *Vogt Manufacturing Company*, 227 N. Y. 468, 472 (1920); *Matter of Levy*, 249 N. Y. 168, 169 (1928).

3. Under the statute, the lien now attaches from the commencement of the action or suit, thus modifying the common law rule under which the lien did not

arise until judgment was recovered. *Matter of Heinsheimer, supra*, p. 365.

4. The statute is all-inclusive in its language and contains no exception in favor of a Trustee in Bankruptcy or anyone else—it "has provided a lien in all cases." *Robinson* v. *Rogers*, 237 N. Y. 467, 472 (1924).

5. The right to the lien is not dependent upon proof that there is no other adequate security. It exists in every instance "and not merely where the client fails to provide some other form of security or protection, and the courts cannot themselves substitute another form of protection for that provided in the statute." *Robinson* v. *Rogers, supra*, p. 472.

6. The lien is recognized by the Federal Courts and is not invalidated by bankruptcy. *In re Baxter & Co.*, 154 Fed. 22, 25 (C. C. A. 2d, 1907); *In re Badger*, 9 F. (2d) 560 (C. C. A. 2d, 1925); *In re San Juan Gold, Inc.*, 96 F. (2d) 60 (C. C. A. 2d, 1938); *Nic Projector Corp.* v. *Movie-Jecktor Co.*, 16 F. Supp. 605 (S. D. N. Y. 1935); *In re Pyrocolor Corp.*, 46 F. (2d) 554 (S. D. N. Y., 1930).

7. Where an attorney has not been discharged for good cause he may enforce his lien immediately, his right to payment being on a *quantum meruit* basis. *Matter of Krooks*, 257 N. Y. 329 (1931); *Matter of Tillman*, 259 N. Y. 133 (1932); *Matter of Weitling*, 266 N. Y. 184 (1935); *Matter of Montgomery*, 272 N. Y. 323 (1936); *Martucci* v. *Brooklyn Children's Aid Society*, 284 N. Y. 408 (1940).

8. The attorney's lien is determinable and enforcible in the court in which suit was brought and where the attorneys' services were rendered. *Goodrich* v. *McDonald, supra*; *Matter of King*, 168 N. Y. 53 (1901).

In a word, as Mr. Justice WALTER pointed out (R. 104), the essence of the charging lien is "a right in the attorney

to have the court in which the client's suit was brought so to control its own judgments and processes as to see that the attorney is paid before the client gets any recovery into his own hands."

The fixed policy of the New York courts has been to construe the statute liberally in the interests of the attorneys sought to be protected. *Fisher-Hansen* v. *Brooklyn Heights R. R. Co.*, 173 N. Y. 492 (1903).

An apt illustration of the applicability of this section to an administrator or trustee acting under appointment in another state is found in *Matter of King*, 168 N. Y. 53 (1901), in which a New Jersey testamentary trustee commenced an action in the Supreme Court of New York and succeeded through his New York attorney in recovering certain securities which had been wrongfully hypothecated. He then sought to remove these securities from the State without paying his attorney. A proceeding was instituted by the attorney to fix and enforce his lien, and the trustee contended that the New York court lacked jurisdiction. The Court of Appeals, upholding the contention of the attorney, stated (pp. 59-60):

> "The trustee now desires to remove the securities from this state into the state of New Jersey. The securities are under the custody and control of the courts of this State * * *. The services of the attorneys claiming the lien were rendered in this state in an action pending in the courts of this state, resulting in a recovery of the property now sought to be charged with the lien. Our courts have jurisdiction thereof, and now have the power to determine what is fair and reasonable compensation and the amount for which the lien should be established."

See also:

Matter of Atterbury, 222 N. Y. 355 (1918).

B. A Trustee in Bankruptcy coming into the State Court is subject to the same conditions as any other litigant.

It has been consistently recognized that a federal trustee in bankruptcy or a trustee in reorganization who becomes an active litigant in a state court occupies the same status as any other litigant.* *Remington on Bankruptcy*, 4th Ed., Vol. 5, Sec. 2131, pp. 243-244; *Ohio Oil Co.* v. *Thompson*, 120 F. (2d) 831 (C. C. A. 8th, 1941), *cert. den.* 314 U. S. 658 (1941); see *Boteler* v. *Ingels*, 308 U. S. 57 (1939); *Foust* v. *Munson S. S. Lines*, 299 U. S. 77, (1936); *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478 (1940).

In *Ohio Oil Co.* v. *Thompson*, *supra*, the Court (THOMAS, C. J.) stated (p. 836-7):

> "It has often been affirmed in cases of bankruptcy that, although the courts of the United States have exclusive jurisdiction 'of all matters and proceedings in bankruptcy', or, as stated in the opinion of the Supreme Court in this case, 'an exclusive and non-delegable control over the administration of an estate in its possession', when a trustee, having been given authority to do so, appears in a state court to litigate his right to property the state court has jurisdiction of all the incidents of the litigation, and its judgment in such action is binding upon him [Citing cases including *Sherman* v. *Buckley*, 119 F. (2d) 280 (C. C. A. 2d, 1941) *cert. den.* 314 U. S. 657 (1941).]"

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* Even the Government of the United States, which is immune from suit without its consent, upon voluntarily becoming a party to a legal proceeding "submits to the application of the same principles by which justice is administered between private suitors" (*The Siren*, 7 Wall. 152 [1869]); or, as Mr. Justice HOLMES stated: "When the United States comes into court to assert a claim, it so far takes the position of a private suitor as to agree by implication that justice may be done with regard to the subject matter." *U. S. v. The Thekla*, 266 U. S. 328, 339-340 (1924); see other cases cited by Mr. Justice WALTER (R. 99).

Consonant with the rule thus expressed, it has been held that a trustee in bankruptcy is liable as any other litigant for fees and costs (*In re Neely*, 113 Fed. 210 [C. C. A. 2d, 1902]); he is bound by all adjudications made in the state court proceedings (*Fischer* v. *Pauline Oil & Gas Co.*, 309 U. S. 294 [1940]; *Schoenherr* v. *Van Meter*, 215 N. Y. 548 [1915]; *Arkansas Corp. Commission* v. *Thompson*, 313 U. S. 132 [1941]; *Winchester* v. *Heiskell*, 119 U. S. 450 [1886]; *Davis* v. *Friedlander*, 104 U. S. 570 [1882]); his adversary may interpose counterclaims and set-offs (*Ohio Oil Co.* v. *Thompson*, *supra*); and he may even be found guilty of contempt of the state court (*Stevens Co.* v. *Foley*, 67 Utah 578, 248 Pac. 815 [1926]). It is also clear that all proceedings and processes in the state court to enforce a judgment whether through the sheriff, by supplementary proceedings or otherwise, are available to him.

C. A Trustee in Bankruptcy is subject to State attorneys' lien laws.

As an application of the rule that a trustee appointed under the Bankruptcy Act occupies the same status as another litigant in a state court, it has been expressly held that, if, with the authority of the bankruptcy court, he invokes the aid of the state courts to press a claim in favor of the bankrupt or the estate, he accepts this privilege *cum onere* and submits to the jurisdiction of the state court to fix and determine the liens of the attorneys prosecuting the action. Arguments that this constitutes an interference with the exclusive jurisdiction of the bankruptcy court have been rejected. *Sherman* v. *Buckley*, 119 F. (2d) 280 (C. C. A. 2d, 1941), *cert. den.* 314 U. S. 657 (1941); *Cup Craft Paper Corp.* v. *Federal Paper Board Co.*, 262 N. Y. App. Div. 91 (1941), *aff'd* 289 N. Y. 671 (1942); *In re Cup Craft Paper Corp.*, 40 F. Supp. 927 (S. D. N. Y., 1941), *aff'd sub nom. New York Credit Mens. Assn.* v. *Schlesinger*, 126 F. (2d) 472 (C. C. A. 2d, 1942); *Ohio Oil*

Co. v. Thompson, 120 F. (2d) 831 (C. C. A. 8th, 1941), *cert. den.* 314 U. S. 658 (1941), *supra;* see also *In re Prudence Company, Inc.*, 96 F. (2d) 157 (C. C. A. 2d, 1938), *cert. den.* 305 U. S. 616 (1938).

Sherman v. Buckley

The decision of the Second Circuit Court of Appeals in the *Sherman* case (119 F. [2d] 280), upon which Justice WALTER relied and Chief Judge LEHMAN and Judges LOUGHRAN and CONWAY rested their dissent, is directly in point.

One Gould, by Buckley & Buckley, his attorneys, brought an action in the New York Supreme Court resulting in a judgment dismissing the complaint. In January, 1934, while an appeal was pending, Gould was adjudicated a bankrupt and a trustee (Sherman) was appointed by the District Court in Connecticut. The trustee then procured authorization of his bankruptcy court to proceed with the New York action in the name of the bankrupt, with the understanding that the avails thereof would enure to the benefit of the bankrupt's estate. In 1935, one year after the appointment of the trustee, he determined to substitute other attorneys in place of the Buckley firm. Thereafter, upon motion made by the trustee in the state court, an order was entered granting substitution and fixing the lien of the displaced attorneys at 30% of any recovery obtained in the action. Subsequently the case was settled for $40,000, and the Buckley firm applied to the state court for an order directing defendants to pay them the amount of their lien. The trustee thereupon applied to the bankruptcy court for an order enjoining the attorneys from taking any steps in the state court to enforce their lien. He contended in his application that the state court was "without jurisdiction to adjudicate the value of their [Buckley & Buckley's] lien"; that "the avails of the action belong to the Trustee in Bankruptcy and are within the custody of the United States District Court for

the District of Connecticut" and that the proceeding sought to be enjoined "constitutes an interference with the jurisdiction of that Court in its paramount right to administer the bankrupt's estate" (Rec. on App., ff. 19-24, 31).

The District Court granted the injunction on the ground that the state court had no jurisdiction (Rec. on App., ff. 211-213).

The Circuit Court of Appeals reversed and held that the District Court had no power to interfere with the Buckleys' lien or with their right to have it determined and enforced in the state court. Rejecting the argument of the trustee that the fixing of the lien constituted an interference with the exclusive jurisdiction of the bankruptcy court, the opinion (Judge LEARNED HAND) stated (p. 282):

> "* * * He [the trustee] could of course substitute other attorneys, as he did, and Buckley & Buckley were obliged to retire; but the substitution did not affect their charging lien under §475 of the Judiciary Law of New York, Consol. Laws, c. 30, or their possessory lien upon the papers.
>
> In spite of the fact that the jurisdiction of the bankruptcy court is usually described as 'exclusive', it may consent to have the interests of third persons in property of which the bankrupt had possession, adjudicated in a state court if that is more convenient. *Foust* v. *Munson S. S. Lines*, 299 U. S. 77, 57 S. Ct. 90, 81 L. Ed. 49; *Texas* v. *Donoghue*, 302 U. S. 284, 58 S. Ct. 192, 82 L. Ed. 264; *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, 483, 60 S. Ct. 628, 84 L. Ed. 876; *In re Schulte-United, Inc.*, 2 Cir., 49 F. (2d) 264. As we have said, the trustee got the permission of the bankruptcy court to allow the action to be prosecuted in the state court. That necessarily involved a consent to such incidents as the exercise of that court's jurisdiction might involve, among them that, as a condition upon the substitution of new attorneys, the charging lien of the displaced attorneys must be liquidated."

That this decision involved the identical issues presented here is plain from the petition for certiorari to this Court

by the trustee in the *Sherman* case in which he listed the questions involved, as follows (pp. 30-31):

> "The issues in the instant case raise several questions which are of the utmost importance, so that bankruptcy courts and their officers may know just what acts of theirs would constitute a consent that some other court determine questions which otherwise would rest solely in the jurisdiction of the bankruptcy court.
>
> These questions are as follows:
>
> 1. Where a bankruptcy court consents that a trustee prosecute an action *in personam* in the name of a bankrupt, does such consent carry with it the implied consent that the court in which such action is pending may determine claims to or liens against the proceeds of such action?
>
> 2. Where a trustee institutes, intervenes in, or continues in the name of a bankrupt, a plenary suit *in personam* for money damages, does the trustee thereby submit himself to the jurisdiction of the court in which such suit is instituted or is pending to the extent that such court may determine liens or claims, such as attorneys' liens, against the proceeds of such suit?
>
> 3. Where a trustee, with the consent of the bankruptcy court, allows to be continued in the name of a bankrupt a plenary suit *in personam*, with the understanding that the fruits of such suit shall inure to the benefit of the bankrupt's estate, does he thereby submit himself to the jurisdiction of the court in which such suit is pending so that he is liable for costs, or attorneys' fees, etc.?"

Certiorari was denied by this Court (314 U. S. 657 [1941]).

The decision in the *Sherman* case was applied by the same Circuit Court of Appeals in the *Cup Craft* decision referred to above (126 F. [2d] 472 [1942], *aff'g* 40 F. Supp. 927 [1941]), involving a bankruptcy proceeding under Chapter XI of the Chandler Act. It was also cited and

quoted with approval by the Eighth Circuit Court of Appeals in *Ohio Oil Company* v. *Thompson, supra.* See also *In re Austin,* 42 F. Supp. 889 (E. D. N. Y., 1942).

To avoid the effect of the *Sherman* decision the Trustees attempted to distinguish it from the situation at bar. They are unable to do so.*

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* 1. It was urged that the attorneys in the *Sherman* case were not appointed by the bankruptcy court but by the company that went into bankruptcy. It appears, however, in the *Sherman* opinion that the trustee "procured the consent of the bankruptcy court * * * that the action should be continued in Gould's name." In effect, the *Buckley* firm actually represented the trustee until other attorneys were substituted—a period of one year; and, as Judge HAND stated, "we deal with the case as though he [the trustee] had been openly the party plaintiff".

2. It was further contended that the lien in the *Sherman* case was for services performed prior to bankruptcy, whereas here they were rendered to the Debtor and the Trustees after the institution of the reorganization proceedings. In the first place, since the *Buckley* firm continued to represent the trustee subsequent to his appointment, it must be assumed that the lien fixed by the state court included services rendered after the bankruptcy proceedings and there is nothing in the record to the contrary. Moreover, an examination of the opinion, record and briefs in the *Sherman* case, and the petition for *certiorari* to this Court setting forth the questions presented, quoted above, shows that the fact that services were performed before or after bankruptcy was not the basis upon which the decision was reached. See also *In re Prudence Co.*, discussed *infra*, pp. 22-3, in which concededly the important services performed by the attorney for which the court stated he had a charging lien were rendered subsequent to the institution of the reorganization proceedings and the appointment of the trustees.

3. An effort is made to distinguish the *Sherman* case on the ground that the Attorneys in the case at bar were not discharged but had fully performed their services. First, this is contrary to the facts found by the Supreme Court and the Appellate Division which are supported by the Record. Secondly, the suggestion that an attorney's lien is extinguished upon completion of his services and the entry of judgment, thus permitting unconscionable clients to appropriate the fruits of the attorney's labors, is contradicted by the history of attorneys' liens and the decided cases in New York. See, *e. g.*, *Matter of King*, 168 N. Y. 53, *supra*.

In re Prudence Co.

The principle enunciated in the *Sherman* case was approved in *Re Prudence Company Inc., supra,* which involved a company in reorganization under Section 77B of the Bankruptcy Act (96 F. [2d] 157, *cert. den.* 305 U. S. 616). In that case, at the time of the appointment of the trustees by the bankruptcy court, there was pending a plenary action in the name of the debtor to recover upon a surety bond. The trustees requested the attorney prosecuting the case to consent to continue the litigation upon condition that his fees would be fixed by the bankruptcy court. The attorney refused to accept this condition. The trustees nevertheless permitted the attorney to continue to prosecute the action in the name of the debtor with the intention, as the Court found, "of taking the benefit of any recovery which the debtor might make" (p. 159).

The attorney performed the most important services in connection with the litigation *subsequent* to the institution of the reorganization proceedings and the appointment of the trustees; he tried the action and obtained a substantial judgment.

Judge SWAN, after discussing the lien rights of the attorney, categorically stated (p. 160):

> "Success having been achieved, they [the trustees] can reap the benefit of the judgment, but they take it subject to the attorneys' charging lien."

On the basis of the foregoing authorities it is manifest that the Trustees in the present case are subject to the New York Attorneys' Lien Law by virtue of the fact that the suits were brought in the State Court with the authority of the Bankruptcy Court.

The decision of the Court of Appeals that the State Court is precluded by the Constitution and Chapter X of the Bankruptcy Act from determining and enforcing the lien involves a complete nullification of State lien laws

so far as bankrupts or debtors in reorganization and their trustees are concerned, and clothes them with an immunity from the operation of State laws not possessed by any other litigant. This result is inconsistent with the adjudicated cases and constitutes a radical departure from long-established rules and policy. It finds no support in the express provisions of the Constitution or the federal reorganization statute; nor will such drastic change be implied from any such provisions.* See, *Palmer* v. *Massachusetts*, 308 U. S. 79, 83 (1939); *Emil* v. *Hanley*, 318 U. S. 515, 521 (1943); *Marine Harbor Properties* v. *Manufacturers Trust Co.*, 317 U. S. 78, 83 (1942); *Robertson* v. *Railroad Labor Board*, 268 U. S. 619, 627 (1925); Point IV, *infra*. In the language of this Court† we say:

> "Clearly, means of permitting such immunity from local laws will not be read into the Bankruptcy Act."

POINT II

The attempt by the Trustees to substitute themselves in place of the Attorneys in charge of the suits in the State Court subjected the Trustees to such conditions as that Court might impose, including the fixing and enforcement of the Attorneys' liens.

An additional basis for the jurisdiction of the State Court to fix the Attorneys' liens arises from the acts of the Trustees in seeking to substitute themselves for the Attorneys in the New York suits. This is evidenced by the Trustees' letter to the Attorneys dated June 3, 1941 (R. 22-23). Particular attention is directed to the following language:

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* The federal statutory provisions which it is alleged affected the Attorneys' rights under the New York Judiciary law are discussed in detail Point IV *infra*, p. 36 et seq.

† *Botcler* v. *Ingels*, 308 U. S. 57, 61 (1939).

"* * * we have decided that it is our duty as Trustees to assume the burden ourselves of taking over, preparing and arguing the pending appeals and any additional appeals that may be taken from any judgment that may be entered as a result of the hearings before Referee Dunn. We shall also act directly in the efforts which are being made to collect against C. K. Reynolds, Woodward and others.

* * * we feel compelled to take over all pending matters that are in your hands, except the conduct of the hearings before Referee Dunn.

* * * we shall relieve you henceforth of the burden and responsibility of the litigation. * * *"

The Attorneys in their reply of June 4, 1941 (R. 23-24), addressed to the Trustees, stated in part:

"Nevertheless, * * * we are prepared to accede to your wishes, provided:

1. We are relieved of our responsibilities, and

2. Our fees and disbursements to date are paid in full."

In the stipulation between the Attorneys and the Trustees, marked "So Ordered" by the Bankruptcy Court in the reorganization proceedings (R. 24-26), it was provided:

"Respondents [the Attorneys] will consent to the substitution of petitioners [the Trustees] or other attorneys in place and stead of respondents in all pending actions on behalf of petitioners upon such terms and conditions as shall be fixed by the courts of New York, or * * * by the appropriate court * * *."

It is undisputed that the Attorneys, after the entry of judgment in Action No. 1, ceased functioning as counsel for the Trustees in that action and that all further steps, including the proceedings to collect the judgment and the settlement with some of the defendants, were taken by the Trustees.

Justice WALTER in his opinion held this whole transaction to be an attempt by the Trustees to secure a substitution and supplant themselves (both being engaged in the practice of law) in place of the Attorneys. He stated in overruling the Trustees' objection to the jurisdiction of the State Court that they "cannot avoid such submission by the device of discharging their attorneys even though they refrain from formally moving for the substitution which they in effect seek" (R. 99). Neither the Appellate Division, which affirmed without opinion, nor the Court of Appeals, which reversed on the opinion of Judge FINCH, disturbed this finding in any respect.

In *Sherman* v. *Buckley, supra,* Judge HAND, after referring to the fact that the trustee intended to prosecute the action by new attorneys, stated (p. 282):

> "when he determined to do that, he necessarily subjected himself to the procedure of the state court, of which the substitution of attorneys was a part. He could not insist that new attorneys should represent him in that court without its consent, upon which it might impose such conditions as it saw fit. * * * As we have said, the trustee got the permission of the bankruptcy court to allow the action to be prosecuted in the state court. That necessarily involved a consent to such incidents as the exercise of that court's jurisdiction might involve; among them that, as a condition upon the substitution of new attorneys, the charging lien of the displaced attorneys must be liquidated."

POINT III

Under Section 77B, in effect when Action No. 1 was instituted, jurisdiction over such action and its incidents was never in the Bankruptcy Court but became vested exclusively in the State Court.

In the preceding arguments it has been assumed that the Bankruptcy Court initially had jurisdiction over the causes of action in favor of the Debtor and surrendered its jurisdiction to the State Court.

However, with respect to Action No. 1, the principal action, which was commenced in the State Court while Section 77B was in effect (as distinguished from Action No. 2 and the Globe Action instituted after the effective date of Chapter X, September 22, 1938), it is clear that jurisdiction was never vested in the Bankruptcy Court but became vested exclusively in the State Court. Consequently it was only that part of the assets recovered in the action, less the amount of the Attorneys' charging lien and other costs fixed by the State Court, that ever became subject to administration in bankruptcy.*

Thus, there is an important additional ground, relied upon by Justice WALTER, which sustains the jurisdiction of the State Court to fix the lien in Action No. 1.

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* It should be noted that Action No. 1 can for this purpose be considered independent of the other two actions, for the order below fixed separate liens based upon the particular services rendered in each action, i.e., a lien for $100,000 in Action No. 1; $2,000 in Action No. 2 and $750 in the Globe Action (R. 6-8).

A. Since Action No. 1 was commenced while Section 77B was in effect, the jurisdiction of the Bankruptcy Court must be determined by that section.

The majority of the Court of Appeals adopted the argument of the Trustees and predicated their decision upon the provisions of Chapter X,* which it was claimed expanded the jurisdiction of the Bankruptcy Court beyond prior enactments so as to include causes of action in favor of the Debtor. However, the majority were in error in applying Chapter X to Action No. 1, for Chapter X, though adopted on June 22, 1938, did not become effective until September 22, 1938. Action No. 1 was commenced on August 4, 1938 while Section 77B was in effect.

That Section 77B was the proper statute to test the jurisdiction of the Bankruptcy Court in respect to Action No. 1 is clear. This is important, since it has been held that Section 23 of the Bankruptcy Act (limiting jurisdiction of the bankruptcy court) is applicable to Section 77B. Section 23 is expressly inapplicable to Chapter X.†

In *Re Standard Gas & Electric Co.*, 119 F. (2d) 658, 663 (C. C. A. 3rd, 1941), where a company in reorganization under Section 77B commenced a plenary action against former officers in June, 1938, prior to the effective date of Chapter X, the Third Circuit Court of Appeals held that jurisidiction of the bankruptcy court in respect to such action was determined by Section 77B, MARIS, C. J., stating (p. 663):

> "The provisions of Chapter X are made applicable to reorganization proceedings but are not extended to plenary actions involving controversies at law or in equity instituted before the effective date of that chapter."

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* Pub. L. No. 696, 75th Congress. Approved by the President June 22, 1938. 52 Stat. 840, 883.

† See Bankr. Act, Section 102.

Similarly in *Tilton* v. *Model Taxi Corp.*, 112 F. (2d) 86, 88 (C. C. A. 2d, 1940) (PATTERSON, C. J.), the Circuit Court of Appeals for the Second Circuit stated:

> "* * * In the Chandler Act (11 U. S. C. A. §502) it is provided that section 23 of the Bankruptcy Act shall not be applicable to proceedings under Chapter X, and it may be that the District Court would have jurisdiction of an action of the present sort brought by a trustee appointed under that chapter, even where the defendant did not consent. The Chandler Act did not take effect until after joinder of issue in the present action, and we see no occasion to discuss whether the jurisdiction of the court has been broadened by the later legislation."

These decisions are in conformity with the principle stated in the headnote of the decision of this Court in *Fraenkl* v. *Cerecedo*, 216 U. S. 295 (1910) that: "Jurisdiction is determined as of the time of commencement of the suit, and even though the jurisdiction of the court be enlarged by a subsequent statute so as to include the parties, the Court cannot acquire jurisdiction against objection."

Indeed, it would appear that an interpretation of Chapter X which would give it retroactive operation so as to impair or destroy the Attorneys' liens herein which had previously attached at the commencement of Action No. 1, would render the Federal statute unconstitutional in depriving the Attorneys of property without due process of law.

B. Under Section 77B the Bankruptcy Court had no jurisdiction over *in personam* claims of a debtor against third persons.

1. THE LAW IMMEDIATELY PRIOR TO SECTION 77B.

Before the enactment of Section 77B the rule was well established that causes of action in favor of a bankrupt against third persons for an accounting and personal judgment did not come within the *summary jurisdiction* of the bankruptcy court because it constituted an "adverse claim"

which was not in the possession of that court. *Taubel-Scott-Kitzmiller Co.* v. *Fox,* 264 U. S. 426 (1924); *Kelley* v. *Gill,* 245 U. S. 116 (1917); *Park* v. *Cameron,* 237 U. S. 616 (1915).

Moreover, by virtue of Section 23 of the Bankruptcy Act the bankruptcy court was excluded from entertaining *plenary* jurisdiction over such causes of action. This Court in *Schumacher* v. *Beeler,* 293 U. S. 367, 374 (1934), in an opinion which examined the legislative history and purpose of Section 23, stated:

> "In enacting §23, it was clearly the intent of the Congress that the federal courts should not have the unrestricted jurisdiction of suits between trustees in bankruptcy and adverse claimants which these courts had exercised under the broad provisions of §2 of the Act of 1867. The purpose was to leave such controversies to be heard and determined for the most part in the state courts 'to the greater economy and convenience of litigants and witnesses'."

See also: *Bardes* v. *Haworden Bank,* 178 U. S. 524 (1900); *Bush* v. *Elliott,* 202 U. S. 477, 483 (1906); *Park* v. *Cameron,* 237 U. S. 616 (1915); *Remington* on Bankruptcy, 4th Ed., Vol. 5, Sec. 2189, p. 316.

It is thus clear that while Congress had the power under the constitutional provision relating to bankruptcies to confer upon the bankruptcy court jurisdiction over causes of action in favor of the bankrupt (*Taubel-Scott-Kitzmiller Co.* v. *Fox, supra*), it fixed as its policy, embodied in Section 23, that jurisdiction of such causes of action should be in the state courts except where federal jurisdiction might be otherwise invoked.

2. SECTION 23 AND THE LIMITATIONS UPON THE BANKRUPTCY COURT'S JURISDICTION OVER IN PERSONAM ACTIONS ARE APPLICABLE TO 77B PROCEEDINGS.

Subdivision (k) of Section 77B (48 Stat. 921, 11 U. S. C., § 207[k]) lists several sections of the Bankruptcy Act

which are expressly made inapplicable to reorganization proceedings. Section 23 is not one of the sections so listed. Subdivision (k) further provides that all other provisions of the Bankruptcy Act are applicable "except such as are inconsistent with the provisions of this Section 77B." See *Meyer* v. *Kenmore Granville Hotel Co.*, 297 U. S. 160, 163 (1936); *O'Connor* v. *Mills*, 300 U. S. 26, 27 (1937).

Every Circuit Court of Appeals in which the question has arisen has held that Section 77B was not inconsistent with Section 23 and that the same pre-existing limitations upon the jurisdiction of the bankruptcy court still existed in connection with the enforcement of personal claims in favor of a debtor.

Thus, in *Re Standard Gas & Electric Co.*, 119 F. (2d) 658 (C. C. A. 3d, 1941), a decision directly in point, a trustee of a company in reorganization under Section 77B in the District Court of Delaware commenced an action in that Court prior to the effective date of Chapter X against former officers and directors for breach of their duties as fiduciaries and prayed for an accounting and money judgments. Service of process was made in Delaware upon the resident defendants and service was made upon the non-resident defendants by process issued outside the State. The resident defendants moved to dismiss the complaint on the ground that under Section 23 the District Court did not have jurisdiction of the causes of action. The non-resident defendants also moved to vacate service for lack of personal jurisdiction. The District Court (NIELDS, J.) found that under Section 23 the Court did not have jurisdiction of the suits.*

The Circuit Court of Appeals for the Third Circuit, per MARIS, C. J., in a comprehensive opinion sustained the ruling below.

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* The Court also found that personal jurisdiction had not been acquired over the non-resident defendants and was sustained in that ruling by the Circuit Court.

Addressing himself to a provision in subdivision (a) of Section 77B said to have been inconsistent with Section 23, namely, that the Court had jurisdiction of "property wherever located"—which this Court also had occasion to consider in *Palmer* v. *Massachusetts*, 308 U. S. 79—Judge MARIS stated (pp. 661-662):

> "In a broad sense a claim by a debtor against a third person is property of the debtor. As such the reorganization court may direct its prosecution by the trustee of the debtor if it is appropriate to do so in order to effect the debtor's reorganization. But it is a species of property which may only be realized upon for the benefit of the debtor and its creditors by the successful prosecution of a plenary suit against the third persons involved. We have seen that section 77B does not purport to confer jurisdiction over those persons. Such claims must therefore be enforced by plenary suits brought in courts whose existing jurisdiction is appropriate to entertain them. * * *
>
> It is true that the jurisdiction conferred by section 77B is over the debtor's property 'wherever located,' and that in this respect the section departs from the earlier provisions of section 2, sub. a which restricted the summary jurisdiction of the courts of bankruptcy to 'their respective territorial limits.' Under those earlier provisions it was necessary for a trustee in bankruptcy to institute ancillary proceedings in other districts in order to deal with property of the bankrupt located in those districts. Subdivision (20) of Section 2, sub. a expressly confers such ancillary jurisdiction upon courts of bankruptcy. It was to eliminate the necessity for such expense and time consuming ancillary proceedings that Congress conferred upon the reorganization court jurisdiction over the debtor's property 'wherever located.' This is clear from the legislative history of the Act of June 7, 1934, c. 424, 48 Stat. 912, which added Section 77B to the Bankruptcy Act" [footnote, quoting from report of the House Committee on the Judiciary, 73rd Con., 1st Sess., House Report 194]. We think it is equally clear that Congress did not intend to ignore the distinction theretofore recognized in the Bankruptcy Act between jurisdiction over persons and jurisdiction of property—

between proceedings in personam and in rem—and that subdivision a of section 77B did not affect the existing jurisdiction of the bankruptcy courts over the former or conflict with the restrictions which section 23 placed upon that jurisdiction."

The Court then considered the effect of another provision in subdivision (a) of Section 77B which was also claimed to have been inconsistent with Section 23, i.e., that the bankruptcy court shall have the powers of a court appointing a receiver in equity (p. 662):

> "This reference to the powers which a federal equity court exercises when it appoints a receiver is to the substantive powers which such a court exercises over the property in its custody rather than to its jurisdiction to entertain plenary suits growing out of the receivership. Finletter, Principles of Corporate Reorganization, page 187. This becomes clear when subdivision a is considered in the light of subdivision o of section 77B which reads: 'In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition or answer was approved.'"

In *Re Prima Co.*, 98 F. (2d) 952 (1938), the Circuit Court of Appeals for the Seventh Circuit reached the same conclusion. To the argument that there was an inconsistency between Section 23 and subdivision (a) of Section 77B, the Court, examining the purpose of this subdivision, stated (p. 958):

> "* * * This was done in order to eliminate cumbersome and expensive ancillary proceedings, and to enable the court to operate the property and conduct the business of the debtor pending the reorganization. Moreover, a construction extending the jurisdiction of the District Court to all controversies between the

debtor and adverse party claimants would, to the extent of the operations of section 77B, amount to a repeal by implication of section 23. It is not contended that there is an express repeal and we think subdivisions (k) and (o), 11 U. S. C. A., § 207(k, o), clearly negative a repeal by implication."

Certiorari was denied by this Court *sub. nom. Keig* v. *Harris Trust & Savings Bank*, 305 U. S. 658 (1939).

In *Re Prudence Bonds Corp.*, 75 F. (2d) 262 (1935), Judge LEARNED HAND of the Circuit Court of Appeals for the Second Circuit observed (p. 263):

"It is clear both from the language used in these subdivisions [(a) and (o)] and from the consequences of a contrary ruling, that Congress did not intend the bankruptcy court in proceedings under section 77B to take over all litigation between the debtor and third persons."

In *Thompson* v. *Terminal Shares, Inc.*, 104 F. (2d) 1 (1939), the Eighth Circuit Court of Appeals, per SANBORN, C. J., reaffirmed the rule in the preceding cases, stating (p. 6) that a court of bankruptcy in proceedings under Section 77B "is without power to bring into the bankruptcy proceedings adverse claimants, whether within or without the district."

The Court further held that the same rule obtained under Section 77, relating to reorganization of railroads, whose legislative history was parallel to that of Section 77B (p. 9):

"* * * We think that the jurisdiction conferred by Section 77 upon the courts of bankruptcy is not to be regarded as general, plenary, nationwide jurisdiction at law and in equity over all questions incident to the collection of the claims of the debtor against third persons, but is to be considered as the traditional jurisdiction of such courts over the property of a bankrupt, wherever located, freed, however, from those limitations which made ancillary proceedings in other

districts necessary, and with the powers which Federal equity courts exercise in receivership proceedings, so far as those powers may be necessary or appropriate in order to preserve and safeguard the property in the actual or constructive possession of debtors and in order to carry on their business pending reorganization."

Certiorari was denied by this Court, 306 U. S. 652 (1939).

See also: *Tilton* v. *Model Taxi Corp.*, 112 F. (2d) 86 (C. C. A. 2d, 1940), *supra; In re Mount Forest Fur Farms of America, Inc.*, 122 F. (2d) 232 (C. C. A. 6th, 1939); *United States* v. *Tacoma Oriental S. S. Co.*, 86 F. (2d) 363 (C. C. A. 9th, 1936); *Finletter*, Principles of Corporate Reorganization (1937), pp. 186-187.

It is thus clear that the Bankruptcy Court under Section 77B did not have either plenary or summary jurisdiction to entertain the causes of action in favor of the Debtor.

In addition to this lack of jurisdiction over the subject matter, the Bankruptcy Court's jurisdiction over such causes of action was further limited in the following essential respects:

1. It could not obtain personal jurisdiction over non-resident defendants because its process could not extend beyond its own territorial borders. See discussion of this point by MARIS, J., in *In re Standard Gas & Electric Company, supra*, pp. 663-665; see also, *Bovay* v. *H. M. Byllesby & Co.*, 88 F. (2d) 990 (C. C. A. 5th, 1937).

2. The appointment of a trustee for a debtor did not operate to stay pending suits in the state court such as Action No. 1 commenced prior thereto; nor did the Trustee by the mere fact of his appointment become a party to every lawsuit in which the Debtor was a plaintiff. If he desired to share in the recovery of any such suit he was permitted under Section 11(c) of the Bankruptcy Act, which was applicable to 77B proceedings, to be substituted as a party plaintiff in the State suit "with like

force and effect as though it had been commenced by him" or to "allow the suit to be continued by the bankrupt and later claim the fruits of any recovery." *In re Prudence Co.*, 96 F. (2d) 157, 159 (C. C. A. 2d, 1938), *cert. den.* 305 U. S. 316 (1938), *supra.*

3. The state court in which the Trustee was compelled to proceed had control of every phase and incident of the suit. For example, it had the power to cause the examination of third parties, to determine whether the claim should be tried by court or jury, to adjudicate the amount owed the Debtor by the third person, to impose statutory costs and fees on all parties, including the Trustee, to issue execution and to invoke proceedings supplementary to execution.

Since, therefore, the State Court legally and actually had sole power and jurisdiction over Action No. 1, Justice WALTER was entirely correct in stating (R. 107) that:

> "It is, indeed, a little short of an absolute contradiction to say that a bankruptcy court has possession of something which the trustee must go into another court in order to get."

It would therefore seem to follow conclusively that Judge FINCH was in error when he stated that the causes of action constituted assets within the exclusive jurisdiction of the Bankruptcy Court and that the New York lien proceedings invaded that jurisdiction. To the contrary, Action No. 1 was within the exclusive jurisdiction of the State Court from the moment it was instituted, and it was only that part of the funds recovered in the action which remained after the deduction of the amount of the charging lien and other statutory costs that ever became an asset subject to the Bankruptcy Court's jurisdiction. This is in exact accord with *In re Prudence Co.*, discussed above, pp. 22-3, in which the Second Circuit Court of Appeals, referring to a plenary suit in favor of a debtor in 77B proceed-

ings, stated: "Success having been achieved, they [trustees] can reap the benefit of the judgment, but they take it subject to the attorney's charging lien." Similarly, in *Re Bay Ridge Inn*, 94 F. (2d) 555, 557 (C. C. A. 2d, 1938), in which a trustee in bankruptcy claimed that the bankruptcy court had jurisdiction of a claim for refund against the New York Liquor Authority, the following language of Judge AUGUSTUS HAND is particularly apposite:

> "The refund is not an asset in the hands of the bankrupt unless and until the Authority, subject to review by the New York court, shall award it to the trustee in accordance with the terms of the act. The right to reinstatement or to a refund depends wholly upon the action of the state tribunals and is in no way within the control of the bankruptcy court. Any rights or privileges of the trustee were created by the New York Legislature and were subject to such conditions as it might impose."

In conclusion, it is submitted that in Action No. 1 (the principal suit) the determination of the Attorneys' lien by the State Court could not invade the exclusive jurisdiction of the Bankruptcy Court for two reasons: First, this cause of action was not within the jurisdiction of the Bankruptcy Court; second, if it were, that Court surrendered its jurisdiction to the State Court by directing the prosecution of the suit there.

POINT IV

Neither the Constitution nor the Federal reorganization statutes prohibit the State Court from fixing liens upon causes of actions prosecuted in that Court with the authorization of the Bankruptcy Court.

The decision of the Court of Appeals is predicated solely upon the ground that the causes of action in favor of the Debtor were assets within the jurisdiction of the Bank-

ruptcy Court by virtue of Chapter X of the Bankruptcy Act and that the fixing of attorneys' liens by the State Court invades this jurisdiction. In reaching this result the majority adopted the argument advanced by the Trustees that Congress through the enactment of Chapter X has greatly expanded the jurisdiction of the Bankruptcy Court.

The effect of this decision is that Chapter X has completely nullified the local Attorneys' Lien Law and has conferred upon debtors in reorganization and their trustees who invoke the aid of New York courts a unique immunity from the State's laws to that extent.

Congress never intended any such result either by Section 77B or Chapter X.

A. Section 77B, not Chapter X, is applicable to Action No. 1. Under it there is no immunity to Trustees from local lien laws.

As shown above (Point III) Action No. 1 was commenced while Section 77B was in effect; yet the Court of Appeals erroneously considered the jurisdiction of the Bankruptcy Court as being under Chapter X instead of Section 77B. We have pointed out that Congress in the enactment of Section 77B did not depart from its long-established policy of having the state court, not the bankruptcy court, exercise jurisdiction of causes of action in favor of a bankrupt or debtor against third persons.

Prior to the enactment of Chapter X it was thus clear, as evidenced by the *Sherman*, *Prudence* and other authorities discussed *supra* (Point I), that the trustee in bankruptcy or reorganization was subject to the local attorneys' lien laws.

B. Chapter X has not conferred upon trustees in reorganization immunity from attorneys' lien laws.

Neither the majority of the Court of Appeals nor the Trustees was able to refer to a single provision in Chapter

X which effects the alleged radical change in the pre-existing law and precludes a state court from fixing liens upon causes of action prosecuted there with the authorization of the bankruptcy court. There is, of course, no such provision.*

In the absence of any express provision conferring an immunity upon trustees, the majority of the Court of Appeals was compelled to reach such result by implication from several sections of Chapter X. This was in direct violation of the admonitions of this Court that "Clearly, means of permitting such immunity from local laws will not be read into the Bankruptcy Act" (*Boteler* v. *Ingels*, 308 U. S. 57, 61 [1939]) and that "it is not lightly to be assumed that Congress intended to depart from a long established policy." *Robertson* v. *Railroad Labor Board*, 268 U. S. 619, 627 (1925); *Panama Railroad Company* v. *Johnson*, 264 U. S. 375, 384 (1924); *In re East River Towing Co.*, 266 U. S. 355, 367 (1924).

The attitude of this Court was recently expressed in *Emil* v. *Hanley*, 318 U. S. 515, 521 (1943):

> "We cannot help but think that if Congress had set out to make such a major change, some clear and unambiguous indication of that purpose would appear."

Again in *Palmer* v. *Massachusetts*, 308 U. S. 79, 83-84 (1939), the Court pointed out that "especially is wariness enjoined when the problem of construction implicates one of the recurring phases of our federalism and involves striking a balance between national and state authority * * *"

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* There is nothing to preclude a trustee under Chapter X from suing in the state courts or being substituted as a plaintiff in a suit instituted there by the debtor prior to the reorganization proceedings. On the contrary, this is expressly permitted by Section 11, subdivisions (c) and (e) of the Act which is applicable to Chapter X proceedings (Bankr. Act, § 102). When that choice is made, no provision in Chapter X prohibits the state court from obtaining full jurisdiction over the suit and its incidents.

Turning to the provisions upon which the majority of the Court of Appeals based its conclusion, it will be clear that the Court struggled, as did the trustees in *Palmer* v. *Massachusetts, supra,* to derive meaning "not from specific language but by fashioning a mosaic of significance out of the innuendoes of disjointed bits of a statute", with the result that "what professes to be mere rendering becomes creation and attempted interpretation of legislation becomes legislation itself" (p. 83):

1. Great reliance was placed by the majority upon Section 111, which provides that the bankruptcy court shall "have exclusive jurisdiction of the Debtor and its property wherever located" (R. 125). This is not a new provision; it is a repetition of the exact words in subdivision (a) of Section 77B. Its purpose as shown above, pp. 31-4, was to eliminate ancillary receiverships.

Only recently this Court in *Palmer* v. *Massachusetts, supra,* pp. 85-6, rejected a contention that the identical clause in Section 77 gave power to the bankruptcy court to supplant a relevant State administrative tribunal in its decision relating to property belonging to the debtor in reorganization.

2. Section 114 was referred to, under which the jurisdiction of the bankruptcy court in Chapter X proceedings shall be the same as in bankruptcy proceedings upon adjudication. This provision also is not new. It "is patterned upon Section 77B(o) and does no more than simplify the language of the law." Senate Report No. 1916, Committee on the Judiciary, May 27, 1938, p. 24. That this section did not enlarge the jurisdiction of the bankruptcy court was expressly held in *Re Prudence Bonds Corp.*, 75 F. (2d) 262, 263 (C. C. A. 2d, 1935), *supra,* and in *Re Standard Gas & Electric Co.*, 119 F. (2d) 658, 662, *supra.*

3. The Court of Appeals referred to Section 256 of the Judicial Code (28 U. S. C. 371), which provides that the

Federal Court shall have exclusive jurisdiction of matters pertaining to bankruptcy, and cited the decisions of this Court in *Gross* v. *Irving Trust Co.*, 289 U. S. 342 (1933); *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734 (1931), and *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478 (1940). Neither this section, which incidentally has been on the statute books since 1911,* nor any of these decisions militate against the operation of the New York Attorneys' Lien Law. They merely enunciate the undisputed proposition that once bankruptcy has intervened, the jurisdiction of the bankruptcy court is exclusive. They do not imply that after the bankruptcy court has assumed its exclusive jurisdiction it cannot consent or authorize the institution of proceedings in a state court. The contrary is the case. Thus, in *Isaacs* v. *Hobbs Tie & Timber Co.*, *supra*, this Court, after speaking of the "exclusive" jurisdiction, added the significant qualification "save by consent of the bankruptcy court" (p. 739). Likewise in *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, 483, this Court, after referring to the "exclusive and non-delegable control over the administration of an estate in its possession", continues in the next sentence, "But the proper exercise of that control may * * * lead the bankruptcy court to consent to submission to state courts of particular controversies * * *." Or, as was stated in *Ex parte Baldwin*, 291 U. S. 610, 619 (1934), "Moreover, the bankruptcy court might, in the exercise of its discretion, conclude that it is desirable to have the litigation proceed in the state court." Indeed, it has been held that the refusal of a bankruptcy court to allow state courts to determine certain questions arising in connection with bankruptcy matters may constitute an abuse of discretion. *Foust* v. *Munson S. S. Lines*, 299 U. S. 77 (1936); *State of Texas* v. *Donoghue*, 302 U. S. 284 (1937).

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* R. S., § 711, March 3, 1911, c. 231, § 256; 36 Stat. 1160.

4. The opinion of the Court of Appeals finally refers to miscellaneous sections of Chapter X (Secs. 241-250) relating to the power of the bankruptcy court over fees, expenses and allowances and the conditions which must be complied with for the payment thereof, and to Section 206 permitting interested parties to be heard.

It is manifest that these sections as well as Section 62, the corresponding section applicable to straight bankruptcy, relate solely and exclusively either to allowances for services rendered within the bankruptcy court itself, e. g., in connection with a plan of reorganization, or to allowances from funds in the possession of the bankruptcy court. There is nothing in these provisions which refers to or tends to limit such *in rem* rights as attorneys may have under local law upon actions and the proceeds thereof within the jurisdiction and custody of the state court. Nor did Congress intend these sections to have any such effect, as is evidenced by the description, derivation and purpose of the sections contained in Senate Report No. 1916 of the Judiciary Committee dated May 27, 1938, in connection with the Chandler Bill, quoted in the margin.* This is further demonstrated

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* "COMPENSATION AND ALLOWANCES:

Section 241, derived in part from section 77B(c)(9), vests the judge with the power to make allowances, for services and for costs and expenses, to referees, special masters, trustees and their attorneys, and to attorneys for the debtor and for petitioning creditors. The latter may themselves be allowed only their proper costs and expenses. Sections 40 and 48 of the act, as relating to the compensation of referees and trustees, are made inapplicable to this chapter.

Section 242, derived in part from section 77B(c)(9), vests the judge with the power to make allowances to any parties in interest, to security holders' representatives, and to their respective counsel and agents, for services rendered or disbursements incurred in connection with the administration of the estate or with a plan approved by the court. These may be made, in the discretion of the judge, even though the plan may not be confirmed, and a liquidation is directed or the proceeding is dismissed.

Section 243 empowers the judge to grant allowances to creditors and stockholders, and their attorneys, for services and expenses incurred in connection with their submission of plans or suggestions therefor, or their objections to confirmation of a plan, or the admin-

by the fact that in spite of the existence of Section 62 it was held in *Sherman* v. *Buckley*, and the other authorities discussed in Point I, that jurisdiction to fix charging liens of attorneys on causes of action was lodged in the state court and not in the bankruptcy court.

As an indication that Congress, in the enactment of Chapter X, and particularly the sections governing allowances, intended to preclude the state courts from fixing

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istration of the estate. These must contribute to the plan confirmed or to the refusal of confirmation of a plan, or be beneficial to the administration of the estate, if such allowance is to be granted.

Sections 244 and 245 deal with compensation and reimbursement for services and expenses in a bankruptcy proceeding which is superseded by a reorganization proceeding.

Section 246 deals with compensation and reimbursement for services and expenses in the event of dismissal or liquidation ordered in the reorganization proceedings.

Section 247 deals generally with hearings, and adequate notice with respect thereto, in the matter of allowances under this article.

Section 248 provides that where a reorganization proceeding supersedes a bankruptcy proceeding, and the former is then dismissed and bankruptcy proceeded with, allowances in the bankruptcy proceeding are to be governed by the rules applicable to such type of proceeding.

Section 249 forbids the granting of allowances to persons acting in a representative or fiduciary capacity who deal in securities of the debtor during the pendency of proceedings under this chapter, except as the judge may approve or consent to an acquisition or transfer thereof in an unusual case. This section is in the main a codification of the rule already imposed by the courts in proceedings under section 77B.

Section 250, derived from section 77B(c)(9), is intended to facilitate appeals from the grant or refusal of an allowance of compensation. These are to be disposed of without the necessity of a printed record. * * *

Section 206, derived in part from section 77B(c), gives any creditor or stockholder, any indenture trustee, and the debtor, the right to be heard on all matters in the proceeding. Existing restrictions on such right to be heard are eliminated as being undesirable. It also allows a labor union of employees of the debtor, in the discretion of the judge, to be heard on the economic soundness of the plan affecting the interests of the employees."

See also H. Report No. 1409 of Mr. Chandler of the Committee on Judiciary, 75th Congr., 1st Sess., July 29, 1937, pp. 45-46.

the liens, Judge FINCH suggested that a contrary ruling would put the disposition of the bankrupt's assets into the hands of a tribunal concerned solely with the rights of the litigants before it, unrestrained by provisions for notice to other interested parties, and unfamiliar with the status of the bankrupt's estate. This is hardly an answer to the question of whether Chapter X was intended to grant immunity to bankruptcy trustees from the operation of the New York Attorneys' Lien Law. Nevertheless, the result so envisioned is neither unusual nor dangerous. Thus, when a trustee brings a plenary suit in a state court against the bankrupt's debtor, the latter may plead and prove any counterclaim that would have been permitted against the bankrupt, so long as it does not interfere with property in the possession of the bankruptcy court or violate the restraint of an order of such court. And the determination by the state court of the merits of the counterclaim is just as binding upon the trustee and the bankrupt's estate as if the counterclaim had been heard and allowed by the bankruptcy referee upon notice to all interested parties to the bankruptcy. (See in addition to authorities cited *supra*, pp. 16-17, *Northeastern R. E. Sec. Corp.* v. *Goldstein*, 276 N. Y. 64 [1937]). Yet neither Congress in the Bankruptcy Act and the amendments thereto, nor any court in construing them, has held such a determination to be fraught with danger to the safeguards provided for in the Bankruptcy Act in the hearing and allowance of claims. It is, of course, indisputable that the trustee as the duly constituted representative of all the parties is in the position to present in the state court any matter tending to reduce or defeat the claim on the merits.

It is thus clear that the drastic change of nullifying local attorneys' lien laws cannot be found in any of the provisions of Chapter X either expressly or by implication. Moreover, the legislative reports accompanying Chapter X are barren of any complaints that the lack of jurisdiction of the bankruptcy court over liens upon causes of action prosecuted in the state courts had prejudicially

affected reorganization proceedings or that the proposed amendments relating to jurisdiction were intended to confer any additional powers upon courts of bankruptcy in such respect. This is an extremely significant circumstance for a matter is "not within the statute unless it be within the intention of the makers." *Thompson* v. *Terminal Shares, Inc.*, 104 F. (2d) 1, 8 (C. C. A. 8th, 1939), *supra*. Furthermore, none of the text writers who have analyzed the changes made by Chapter X has intimated that the major changes relied on by the Court of Appeals and by the Trustees were effected.*

Finally, the decision of the Court of Appeals if permitted to stand leads to highly undesirable consequences never anticipated by Congress. It amounts to an unwarranted federal interference with local authority which, according to this Court's decision in *Palmer* v. *Massachusetts, supra,* should be carefully avoided. It results in a division of jurisdiction between the state and federal courts over actions prosecuted in the former courts, in that the state courts will control many of the phases of the litigation while the federal court will retain control over one of the important incidents, that of determining the charging lien of the local attorney upon the action. This Court in *Emil* v. *Hanley, supra,* unequivocally stated that "an interpretation which leads to a division of authority so fraught with conflict will not be readily implied" (p. 521).

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* *Finletter*, The Law of Bankruptcy Reorganization (1939), Chap. 3, p. 115 *et seq.*; *Douglas*, Improvement in Federal Procedure for Corporate Reorganizations, 24 Amer. Bar Assn. Journal, p. 875 (November 1938); *Weiner*, Corporate Reorganizations under the Chandler Act, 72 U. S. Law Rev., p. 388 (July 1938); *Doub*, Corporate Reorganizations under Chapter X of the National Bankruptcy Act, 3 Maryland L. Rev., p. 1 (Dec. 1938); *Teton*, Reorganization Revised, 48 Yale L. Journal, 573 (Feb. 1939); *Laporte*, Changes in Corporate Reorganization Procedure, proposed by the Chandler and Lea Bills, 51 Harv. L. Rev., p. 672 (February 1938); *Gerdes*, Changes Effected by Chapter X of the Bankruptcy Act, 52 Harv. L. Rev., p. 1 (Nov. 1938).

While Congress unquestionably had the power to effect such an undesirable result it did not do so. As this Court (per Mr. Justice DOUGLAS) stated in *Marine Harbor Properties* v. *Manufacturers Trust Co.*, 317 U. S. 78, 83 (1942):

> "The federal bankruptcy power is, of course, paramount and supreme and may be so exercised by Congress as to exclude every competing or conflicting proceeding in state or federal tribunals. Kalb v. Feuerstein, 308 U. S. 433. In fashioning Chap. X Congress, however, did not go so far."

POINT V

The determination and enforcement of the Attorneys' liens by the State Court is not inconsistent with any alleged contract or agreement made by the Attorneys with the Trustees or the Bankruptcy Court.

The principal arguments of the Trustees and the majority of the Court of Appeals have been answered in the preceding points. One further contention was advanced by the Trustees which is entirely without foundation.

In an attempt to make it appear that a local and not a federal question is presented on this appeal, the Trustees in their brief in opposition to the petition for *certiorari* (Point I) stated that "The primary issue is not as to whether a state court may enforce a lien for services rendered by attorneys in a state court action, but whether the state court, in determining the amount for which a lien, if any, shall be enforced, *must* disregard the contract of the attorneys under which they agreed that the amount of their compensation would be fixed by the federal reorganization court"; and they urged that the lien granted the Attorneys under Section 475 of the Judiciary Law was waived by such contract, which is permissible under Section 474 of the Judiciary Law. The contract according to the Trustees is to be found in the Plan of Reorganization of the Debtor and the orders of the Bankruptcy Court confirming the Plan.

It should be pointed out that any claim of contract was a matter of defense to be pleaded and proved at the trial. Such contention, therefore, cannot properly be considered, as it goes to the merits of the lien and not to the jurisdiction of the State Court to fix the lien or the jurisdiction of this Court to entertain certiorari.

In any event, the contention based upon such alleged contract was urged in the State Court and expressly overruled by Justice WALTER (R. 108-109) and the unanimous affirmance of the Appellate Division. These findings were undisturbed by the Court of Appeals.

Considering the question *de novo*, there are three conclusive answers given by the State Court to the argument that an actual agreement was made by the Attorneys through the adoption of the Plan of Reorganization: (1) The Attorneys were never parties to the Plan of Reorganization or the order confirming it; (2) there is nothing in the Plan, which was promulgated one and a half years after Action No. 1 was instituted and consummated two years thereafter, purporting to affect or destroy the lien rights of the Attorneys which crystallized from the commencement of action; and (3) the discharge and substitution of the Attorneys cancelled any such alleged agreement had there been one.

1.

The Attorneys were never parties to the Plan of Reorganization. They participated in the reorganization proceedings and recommended the adoption and confirmation of the Plan *solely* in their capacity as counsel respectively for the principal debenture and preferred stockholders' committees (R. 55-56, 68-69). Moreover, the compensation which they received in the reorganization proceedings was solely for services rendered as attorneys for their respective committees in those proceedings and had no relation to their services in the New York actions.

2.

The Trustees cannot refer to a single provision in the Plan of Reorganization or the orders of the Bankruptcy Court confirming the Plan which can possibly be construed to nullify and destroy the lien rights of the Attorneys which under Section 475 of the Judiciary Law had attached many months before. At the time of the promulgation and confirmation of the Plan no question of the enforcement by the Attorneys of their liens upon the New York suits was considered or contemplated: It did not arise until June 3, 1941, almost a year after the Plan was confirmed, when the Attorneys were relieved of their duties.

The provision of the Plan upon which the Trustees principally relied is the one with respect to the right of the Bankruptcy Court to fix reasonable compensation to be paid to the Attorneys and their Trustees in connection with the prosecution of the claims of the Debtor. It is apparent that this section merely incorporates Section 241 of Chapter X referred to above, which provides that the Bankruptcy Judge may allow "reasonable compensation for services rendered * * * by the Trustee and other officers, and the attorneys for any of them." As shown above, this section of Chapter X and Section 62(d), the correlative section applicable to straight bankruptcy proceedings, which are embodied in the provision of the Plan, are concerned with the payment of compensation for services rendered within the Bankruptcy Court, or with applications for allowance from funds and assets within the custody and possession of the Bankruptcy Court. They are not concerned with the lien rights of the Attorneys upon specific *res*, the suits and proceeds thereof which are within the jurisdiction and custody of the State Court.

3.

Assuming the Attorneys had entered into an agreement to look solely to the Bankruptcy Court for their compensation, such alleged agreement was cancelled by their discharge and attempted substitution. Under the New York law, while a client has an absolute right to discharge his attorney without cause at any time, nevertheless, if he exercises this privilege, it operates to cancel any agreement which it is claimed existed and entitles the attorneys to have their liens fixed immediately by the Supreme Court on a *quantum meruit* basis under Section 475 of the Judiciary Law. *Matter of Tillman*, 259 N. Y. 133 (1932); *Matter of Weitling*, 266 N. Y. 184 (1935); *Matter of Montgomery*, 272 N. Y. 323 (1936).

As the Court of Appeals stated: "A client may at any time for any reason which seems satisfactory to him, however arbitrary, discharge his attorney [citing cases]. Even in the presence of a definite agreement the client's right persists. Cancellation by him cannot constitute a breach of contract, for implied in every such agreement is the right to discharge" (*Matter of Krooks*, 257 N. Y. 329, 331-332 [1931]). "The client is entitled to cancel his contract of retainer but such an agreement cannot be partially abrogated. Either it wholly stands or totally falls * * *" (*Matter of Tillman, supra*, pp. 135-136).

The Trustees contended that the Attorneys were not discharged but had completed the services for which they were retained. This contention was advanced in spite of the fact that (1) in Action No. 1 the Attorneys were notified that the collection of the judgments (the most important phase of all) was not to be handled by them but by the Trustees, and (2) in Action No. 2 and the Globe Action the Attorneys were relieved of their duties while the actions were still pending untried.

The Trustees urged that the authority of an attorney ceases upon entry of judgment. It is well settled under the New York law that an attorney's authority to represent

a party does not end upon entry of the judgment but continues to include the usual steps to collect the judgment and thereby accomplish the purpose of the retainer. *Ohlquist* v. *Nordstrom*, 143 N. Y. Misc. 502 (1932), *aff'd* 238 N. Y. App. Div. 766 (1933), *aff'd* 262 N. Y. 696 (1933). The Court of Appeals in *Larkin* v. *Frazier*, 224 N. Y. 421, 425 (1918), stated:

> "Under the general authority conferred upon the defendant he was authorized to prosecute the action commenced by him for Clara C. Larkin to final judgment and to enforce collection thereof by the issuance of an execution thereon, to receive the avails of the execution from the sheriff and also to acknowledge satisfaction of the judgment at any time within the statutory period. (*Barber* v. *Dewes*, 101 App. Div. 432, affirmed 184 N. Y. 548; *Read* v. *French*, 28 N. Y. 285; *Bathgate* v. *Haskin*, 59 N. Y. 533; *Steward* v. *Biddlecum*, 2 N. Y. 103.) Likewise he would be authorized to institute proceedings supplemental to execution on the judgment. (*Ward* v. *Roy*, 69 N. Y. 96.) * * * "

CONCLUSION

The order of the Court of Appeals should be reversed and the orders of the Supreme Court affirmed by the Appellate Division should be reinstated.

Respectfully submitted,

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CHARLES ELMORE CROPLEY

Supreme Court of the United States

OCTOBER TERM, 1943

No. 183

B. H. Inness Brown, David Paine, Ethelbert Warfield, et al.,

Petitioners,

vs.

John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW YORK.

APPENDICES TO PETITIONERS' BRIEF

David Paine,
Lawrence S. Greenbaum,
William C. Scott,
Solicitors for Petitioners.

Theodore S. Jaffin,
James F. Dwyer,
of Counsel.

APPENDIX A

Chronology

May 18, 1938	Petitioner for reorganization under Bankruptcy Act filed against Reynolds Investing Co., Inc., in United States District Court, New Jersey (R. 11, 98).
June 22, 1938	Reynolds Investing Co., Inc., by resolution of its board engaged the Attorneys to investigate claims of the company (R. 11).
Aug. 1, 1938	Order by Judge Fake of Bankruptcy Court on application by president of Reynolds Investing Co., Inc., authorizing suit by the corporation through these Attorneys. No provision for payment of fees (R. 12, 98).
Aug. 4, 1938	Suit begun by the corporation in the New York Supreme Court against Reynolds, Woodward et al. (Action No. 1) (R. 12, 98).
Sept. 22, 1938	Chapter X, Bankruptcy Act, became effective.
Jan. 19, 1939	Order of Bankruptcy Court appointing Gerdes and Carpenter Trustees of Debtor and authorizing them to be substituted as plaintiffs in Action No. 1. No provision for payment of fees (R. 12, 98).
Feb. 10, 1939	Order of State Court, on application of Trustees, substituting them as plaintiffs in Action No. 1 (R. 12, 98).

Jan. 16, 1940	Suit commenced by Trustees in the New York Supreme Court against Globe Indemnity Company pursuant to the order of Judge Fake (Globe Action) (R. 19, 98).
May 29, 1940	Suit commenced by Trustees in New York Supreme Court against C. K. Reynolds et al. pursuant to order of Judge Fake (Action No. 2) (R. 16, 98).
June 17, 1940	Order signed by Judge Fake confirming Plan of Reorganization which for the first time included a general provision for payment of fees (R. 62-67, 32-55).
Apr. 24, 1941	Interlocutory judgment by Justice Walter of New York Supreme Court in favor of the plaintiffs in Action No. 1 and directing reference to ascertain damages (R. 14-15, 98).
June 3, 1941	Before completion of hearings before Referee in Action No. 1 and prior to trial of Action No. 2 and Globe Action, Trustees send letter of discharge to Attorneys (R. 20, 22-23, 98-99).
June 20, 1941	Proceedings begun by Trustees before Judge Fake to compel Attorneys to turn over papers (R. 20, 99).
July 9-10, 1941	Motion to turn over withdrawn by Trustees; stipulation signed and "so ordered" by Judge Fake attached to the stipulation authorizing lien proceeding by Attorneys in State Court (R. 21, 24-26, 99).
Nov. 5, 1941	Reference completed (Action No. 1) under the decision of Justice Walter and final judgments entered for the plaintiffs (R. 15).

Dec. 22, 1941	Lien proceedings commenced by Attorneys in State Court (R. 10 et seq.).
Mar. 6, 1942	Order by Justice Walter overruling Trustees' objection to jurisdiction of State Court (R. 4-5).
Mar. 31, 1942	First hearing held by Justice Walter to fix amount of liens (R. 69 et seq.).
Apr. 8, 1942	Second hearing held by Justice Walter to fix amount of liens (R. 85 et seq.).
Apr. 15, 1942	Final order signed by Justice Walter fixing the liens (R. 6-8, 109-113).
June 19, 1942	Appellate Division, Supreme Court, affirmed Justice Walter's orders (R. 118-119).
Apr. 22, 1943	Court of Appeals by vote of 4 to 3 reversed orders of Justice Walter and Appellate Division and dismissed lien proceedings (R. 129-130).
May 27, 1943	Reargument denied by Court of Appeals (R. 130-131).
Oct. 11, 1943	Certiorari granted by U. S. Supreme Court (R. 133).

APPENDIX B

Federal Statutes

JUDICIAL CODE, SECTION 256
(28 U. S. C. 371).

EXCLUSIVE JURISDICTION OF UNITED STATES COURTS.

The jurisdiction vested in the courts of the United States in the cases and proceedings hereinafter mentioned shall be exclusive of the courts of the several States: * * *

Sixth. Of all matters and proceedings in bankruptcy.

Federal Bankruptcy Act

SEC. 23. JURISDICTION: UNITED STATES AND STATE COURTS.

a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings in bankruptcy, between trustees as such and adverse claimants, concerning the property acquired or claimed by the trustees, in the same manner and to the same extent only as though bankruptcy proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the trustees shall only be brought or prosecuted in the courts where the bankrupt, whose estate is being administered by such trustee, might have brought or prosecuted them if proceedings in bankruptcy had not been instituted unless by consent of the proposed defendant, except suits for the recovery of property under section 96, subdivision (b), of this title; section 107, subdivision (e) of this title; and section 110, subdivision (e) of this title.

SEC. 62. EXPENSES OF ADMINISTERING ESTATES; UNAUTHORIZED SHARING OF FEES; WITHHOLDING ALLOWANCES.—a. The ctual and necessary costs and expenses incurred by offiers in the administration of estates shall, except where ther provisions are made for their payment, be reported detail, under oath, and examined and approved or dispproved by the court. If approved, they shall be paid or llowed out of the estates in which they were incurred.

c. A custodian, receiver, or trustee or the attorney or any of them, or any other attorney, rendering services a proceeding under this Act or in connection with such roceeding, shall not in any form or guise share or agree share his compensation for such services with any perpn not contributing thereto, or share or agree to share the compensation of any person rendering services in proceeding under this Act, or in connection with such roceeding, to which services he has not contributed: *Proided, however,* That an attorney-at-law may share such ompensation with a law partner or with a forwarding ttorney-at-law, and may share in the compensation of a aw partner.

d. A custodian, receiver, or trustee or the attorney for ny of them, or any other attorney, seeking compensation or services rendered by him in a proceeding under this ct or in connection with such proceeding, shall file with he court his petition setting forth the value and extent f the services rendered, the amount requested and what llowances, if any, have theretofore been made to him. uch petition shall be accompanied by his affidavit stating hether an agreement or understanding exists between the etitioner and any other person for a division of compenation and, if so, the nature and particulars thereof. If atisfied that the petitioner has, in any form or guise, shared r agreed to share his compensation or in the compensation any other person contrary to the provisions of this subivision, the court shall withhold all compensation from uch petitioner.

SEC. 67. LIENS AND FRAUDULENT TRANSFERS.— • • •

b. The provisions of section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under chapters X, XI, XII, or XIII of this Act, by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

SEC. 111. EXCLUSIVE JURISDICTION OVER DEBTOR AND PROPERTY.

Where not inconsistent with the provisions of this chapter, the court in which a petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and its property, wherever located.

SEC. 114. MATTERS UPON APPROVAL OF PETITION; JURISDICTION, POWERS, AND DUTIES.

Upon the approval of a petition, the jurisdiction, powers, and duties of the court and of its officers, where not inconsistent with the provisions of this chapter, shall be the same as in a bankruptcy proceeding upon adjudication.

SEC. 116. SAME; ADDITIONAL JURISDICTION OVER ADMINISTRATION OF ESTATE.

Upon the approval of a petition, the judge may, in addition to the jurisdiction, powers, and duties hereinabove and elsewhere in this chapter conferred and imposed upon him and the court— • • •

(2) authorize a receiver, trustee, or debtor in possession, upon such notice as the judge may prescribe and upon cause shown, to issue certificates of indebtedness for cash, property, or other consideration approved by the judge, upon such terms and conditions and with such security and priority in payment over existing obligations, secured or unsecured, as in the particular case may be equitable.

SEC. 148. ORDER OF APPROVAL AS STAY OF OTHER PROCEEDINGS.

Until otherwise ordered by the judge, an order approving a petition shall operate as a stay of a prior pending bankruptcy, mortgage foreclosure, or equity receivership proceeding, and of any act or other proceeding to enforce a lien against the debtor's property.

SEC. 206. PERSONS ENTITLED TO HEARINGS.

The debtor, the indenture trustees, and any creditor or stockholder of the debtor shall have the right to be heard on all matters arising in a proceeding under this chapter. The judge may, for cause shown, permit a labor union or employees' association, representative of employees of the debtor, to be heard on the economic soundness of the plan affecting the interests of the employees.

SEC. 216. PROVISIONS OF PLAN.

A plan of reorganization under this chapter— • • •

(2) may deal with all or any part of the property of the debtor;

(3) shall provide for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge; • • •

(10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein; the satisfaction or modification of liens; the cancellation or modification of indentures or of other similar instruments; the curing or waiver of defaults; the extension of maturity dates and changes in interest rates and other terms of outstanding securities; the amendment of the charter of the debtor; the issuance of securities of the debtor or such other corporations for cash, for property, in exchange for existing securities, in satisfaction of claims or stock or for other appropriate purposes; • • •

(13) may include provisions for the settlement or adjustment of claims belonging to the debtor or to the estate; and shall provide, as to such claims not settled or adjusted in the plan, for their retention and enforcement by the trustee or, if the debtor has been continued in possession, by an examiner appointed for that purpose; • • •

SEC. 221. CONFIRMATION BY COURT.

The judge shall confirm a plan if satisfied that—

(4) all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for

costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge;

SEC. 227. EXECUTION OF INSTRUMENTS, SATISFACTION OF LIENS, ETC.

The court may direct the debtor, its trustee, any mortgagees, indenture trustees, and other necessary parties to execute and deliver or to join in the execution and delivery of such instruments as may be requisite to effect a retention or transfer of property dealt with by a plan which has been confirmed, and to perform such other acts, including the satisfaction of liens, as the court may deem necessary for the consummation of the plan.

SEC. 241. PETITIONING CREDITORS; COURT OFFICERS; ATTORNEYS THEREFOR.

The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceedings under this chapter—

(3) by the trustee and other officers, and the attorneys for any of them;

(4) by the attorney for the debtor; * * *

SEC. 242. REPRESENTATIVES AND OTHER PARTIES IN INTEREST; ATTORNEYS THEREFOR.

The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in connection with the administration of an estate in a proceeding under this chapter or in connection with a plan approved by the judge, whether or

not accepted by creditors and stockholders or finally confirmed by the judge—

(1) by indenture trustees, depositaries, reorganization managers, and committees or representatives of creditors or stockholders;

(2) by any other parties in interest except the Securities and Exchange Commission; and

(3) by the attorneys or agents for any of the foregoing except the Securities and Exchange Commission.

SEC. 243. CREDITORS AND STOCKHOLDERS; ATTORNEYS THEREFOR.

The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred by creditors and stockholders, and the attorneys for any of them, in connection with the submission by them of suggestions for a plan or of proposals in the form of plans, or in connection with objections by them to the confirmation of a plan, or in connection with the administration of the estate. In fixing any such allowances, the judge shall give consideration only to the services which contributed to the plan confirmed or to the refusal of confirmation of a plan, or which were beneficial in the administration of the estate, and to the proper costs and expenses incidental thereto.

SEC. 244. PETITION FILED IN PENDING BANKRUPTCY PROCEEDING.

Where a petition is filed under section 127 of this Act, the judge may allow, if not already allowed, reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in the pending bankruptcy proceeding—

(1) by a marshal, receiver, or trustee, as provided in subdivision g of section 48 of this Act, and the attorneys for any of them;

(2) by the attorney for the petitioning creditors;

(3) by the attorney for the bankrupt; and

(4) by any other persons and the attorneys for any of them entitled under this Act to compensation or reimbursement in such bankruptcy proceeding.

SEC. 245. SAME; REFEREE IN BANKRUPTCY.

Where a petition is filed in a pending bankruptcy proceeding, the judge may allow reasonable compensation for services rendered and the proper costs and expenses incurred in such bankruptcy proceeding by a referee in bankruptcy. In fixing such compensation, the judge shall not be restricted by the provisions of section 40 of this Act.

SEC. 246. DISMISSAL OF PROCEEDING OR ADJUDICATION OF BANKRUPTCY.

Upon the dismissal of a proceeding under this chapter, or the entry of an order adjudging the debtor a bankrupt, the judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in such proceeding prior to such dismissal or order of adjudication by any persons entitled thereto, as provided in this chapter, and shall make provision for the payment thereof, and for the payment of all proper costs and expenses incurred by officers in such proceedings.

SEC. 247. HEARING OF APPLICATIONS.

The judge shall fix a time of hearing for the consideration of applications for allowances, of which hearing notice shall be given to the applicants, the trustee, the debtor, the creditors, stockholders, indenture trustees, the Securities

and Exchange Commission, and such other persons as the judge may designate, * * *.

SEC. 248. DISMISSAL OF PROCEEDING AND REINSTATEMENT OF BANKRUPTCY; CHARGING OF ALLOWANCES IN BANKRUPTCY.

In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that a superseded bankruptcy be proceeded with, the compensation allowed by the judge, in the course of the proceeding under this chapter, to the referee, marshal, receiver, or trustee in the bankruptcy proceeding for services rendered by them in such bankruptcy proceeding shall be deemed to have been allowed in such bankruptcy proceeding, and such compensation shall be considered in connection with the making of future allowances therein or shall be readjusted, so as to comply with the provisions of this Act fixing their compensation in a bankruptcy proceeding.

SEC. 249. STATEMENT OF CLAIMS OR STOCK ACQUIRED OR TRANSFERRED AFTER COMMENCEMENT OF PROCEEDING.

Any person seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred.

SEC. 250. APPEALS.

Appeals may be taken in matters of law or fact from orders making or refusing to make allowances of compensation or reimbursement, and may, in the manner and within the time provided for appeals by this Act, be taken to and allowed by the circuit court of appeals independently of other appeals in the proceeding, and shall be summarily heard upon the original papers.

SEC. 256. RIGHT TO PETITION FOR REORGANIZATION DURING PENDENCY OF PRIOR PROCEEDINGS.

A petition may be filed under this chapter notwithstanding the pendency of a prior mortgage foreclosure, equity, or other proceeding in a court of the United States or of any State in which a receiver or trustee of all or any part of the property of a debtor has been appointed or for whose appointment an application has been made.

SEC. 257. TRUSTEE OR DEBTOR IN POSSESSION VESTED WITH RIGHTS OF PRIOR FIDUCIARY.

The trustee appointed under this chapter, upon his qualification, or if a debtor is continued in possession, the debtor, shall become vested with the rights, if any, of such prior receiver or trustee in such property and with the right to the immediate possession thereof. The trustee or debtor in possession shall also have the right to immediate possession of all property of the debtor in the possession of a trustee under a trust deed or a mortgagee under a mortgage.

SEC. 258. PROTECTION OF OBLIGATIONS OF PRIOR FIDUCIARY; PAYMENT OF COSTS AND EXPENSES.

The judge shall make such provision as may be equitable for the protection of the obligations incurred by a receiver or trustee in such prior proceeding and for the payment of the reasonable costs and expenses incurred therein as may be allowed by the judge.

FILE COPY

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B. H. Inness Brown, David Paine, Ethelbert Warfield, et al.,

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ON WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW YORK

REPLY BRIEF OF PETITIONERS AND ANSWER TO BRIEF OF SECURITIES AND EXCHANGE COMMISSION *AMICUS CURIAE*

David Paine,
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of Counsel.

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PART ONE

IN REPLY TO TRUSTEES' BRIEF

The brief of the Trustees fails to meet the essential issue on this appeal and is wholly silent with respect to some of the basic arguments advanced in the Attorneys' brief. Moreover, the legal points raised by the Trustees, some of which have already been anticipated and refuted, either are based on alleged facts at variance with or unsupported by the record facts and findings below, or are utterly without merit.

I

Omissions and failure to meet issue in this case.

1. The Trustees do not dispute the proposition that a bankruptcy trustee coming into a state court is bound as any other litigant by the conditions imposed by the state; nor do they challenge the applicability of the recent pronouncements of this Court in the *Boteler* and *Palmer* cases* that trustees in bankruptcy enjoy no immunity from the operation of State laws.

2. They avoid the main issue (as does the brief of the Securities and Exchange Commission [see pp. 27 *et seq., infra*]) by addressing themselves to the general powers conferred upon the bankruptcy court by the Federal statute to supervise and fix administration costs and expenses and to award compensation or allowances to various individuals. Concession will readily be made that an attempt by the State Court to fix fees for services rendered within the bankruptcy court, such as opposing a claim filed in that court or aiding in the formulation of a plan of reorganization, or to grant an allowance from, or impress a lien upon, funds in the possession of the bankruptcy court would conflict with its exclusive jurisdiction. Yet that is not the problem before this Court, as the State Court here made no such attempt. The issue is whether a debtor in reorganization and then its trustees, who retain New York attorneys to commence and prosecute litigation in the New York court under specific order of the bankruptcy court, are subject to the New York Attorneys Lien Law; that is, does the State Court have power in accordance with a local statute to determine and enforce a lien upon a specific *res*, namely, a cause of action and proceeds thereof which the

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* *Boteler* v. *Ingels*, 308 U. S. 57, 58, and *Palmer* v. *Massachusetts*, 308 U. S. 79, 83-4 (Attorneys' main brief, pp. 16, 38, 39).

Trustees concede they were powerless to reduce to possession, except by suit in the State Court. Applied to actions in New York, the proposition urged by the Trustees would mean that in fulfilling its purpose to permit the bankruptcy court to control administrative costs Congress nullified the power of the State Court to determine the extent of the attorneys' lien under Section 475 of the Judiciary Law, while it left in full force and effect the State statutes which require a trustee in bankruptcy to give security for costs (N. Y. Civil Practice Act, Secs. 1522, 1528); to post an undertaking in the event he desires to attach property, or to obtain an injunction or order of arrest (C. P. A., Sec. 819); to pay the statutory fees for filing papers, sheriff's expenses and witnesses, as well as stenographic charges; or which make him liable to the imposition of additional costs up to $2,000 (C. P. A., Secs. 1512-14). Singly, these may appear to be negligible; together, however, they represent a substantial liability. The Trustees will undoubtedly concede that such statutory costs are fixed by the State and not by the bankruptcy court. It would appear, therefore, that there is no warrant for saying that Congress intended to annul any incident of a State Court litigation.

3. The Trustees make no effectual attempt to refute the cases cited and discussed in Point III of the Attorneys' brief that the provisions of Section 77B, not Chapter X, are applicable to Action No. 1, and that under that Section the bankruptcy court never had custody, possession or jurisdiction of *in personam* causes of action in favor of the debtor. Such causes of action were exclusively within the jurisdiction of the State Court, and it was only that part of the proceeds recoverable in such action less statutory fees and the Attorneys' charging lien—amounting under the New York law to a *pro tanto* assignment of the cause of action—that ever became subject to bankruptcy administration.

II

Statements in Trustees' brief outside, or at variance with, the record and findings below.

A. The alleged contract made by the Attorneys.

The principal argument advanced by the Trustees (Point I) is predicated upon their assertions as "fact" that the Attorneys entered into a contract, embodied in the plan of reorganization and the order of the Bankruptcy Court confirming it, that their fees would be fixed by the Bankruptcy Court which, in effect, constituted a waiver of their lien rights under Section 475 of the Judiciary Law; that they are bound by this contract, and the Court of Appeals so held. The same contention was urged by them in their effort to defeat certiorari on the ground that a question of local law, not of Federal law, was determined below. An examination of the record discloses that the allegation to this effect in the Trustees' answer (R. 27, 31) was specifically denied by the reply interposed by the Attorneys (R. 68). The trial court held that there was no such contract as alleged by the Trustees and decided the issue of jurisdiction on the basis of the applicable Federal statutory provisions. This finding of fact was affirmed by the unanimous decision of the Appellate Division. The Court of Appeals, which is restricted in its jurisdiction by the New York State Constitution to the review of questions of law, not of fact*; could not and did not disturb this finding.

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* "The jurisdiction of the court of appeals, except where the judgment is of death, or where the appellate division, on reversing or modifying a final judgment in an action or a final order in a special proceeding, makes new findings of fact and renders final judgment or a final order thereon, *shall be limited to the review of questions of law;* but the right to appeal shall not depend upon the amount involved." N. Y. Const., Art. 6, § 7; see *Matter of Plass v. The Central N. E. Railway Co.*, 226 N. Y. 449, 450 (1919); *People v. Bellows*, 281 N. Y. 67, 71 (1939).

From an examination of its opinion it is clear that its decision rested wholly upon the ground that the Constitution of the United States and the National Bankruptcy Act conferred an exclusive and non-delegable jurisdiction upon the Bankruptcy Court. The Trustees (Br. 13-14) quote certain language from the opinion of the Court of Appeals to make it appear that the Court determined "as a matter of fact" that the contract alleged by them was entered into. The quoted portion refers solely to that Court's construction of the Bankruptcy Act, which it held formed a part of the contract of the Attorneys. Obviously the determination that certain provisions of the Bankruptcy Act must be deemed to constitute the terms of an implied contract between the Attorneys and the Trustees is not a determination of a question of local law based upon an actual agreement, but rather the determination of a Federal question involving the construction of the Bankruptcy Act.

B. Substitution of the Attorneys.

The Trustees state (p. 6) that after the Attorneys' services were discontinued there was no substitution of the Attorneys and that the Trustees did not appear *pro se* in Action No. 1. This is contrary to the finding of Justice WALTER (R. 99). Neither the Appellate Division, which affirmed without opinion, nor the Court of Appeals, which reversed on the opinion of Judge FINCH, altered or purported to affect this finding in any respect. To test the assertion of the Trustees, one need only inquire how they were able to institute proceedings supplementary to execution for collection of the judgments or to take the legal steps to effectuate the settlement which they refer to, except by substituting themselves for the Attorneys. The fact that the Trustees refrained from formally moving for a substitution which they in effect sought does not alter the matter (R. 99).

C. Alleged abandonment of Globe action and settlement of Action No. 2.

The Trustees assert that the Globe action "has been abandoned; that neither the Attorneys nor the Trustees believe that there is a reasonable prospect of recovery". Further, that Action No. 2 "was settled in conjunction with the settlement of Action No. 1". No word in the record supports these statements. They were anticipated in our main brief (p. 4n). According to the record the Globe action was never abandoned; issue was joined and no steps taken whatever to withdraw or discontinue it at the time the lien proceedings were instituted. Action No. 2 was pending and at issue at the time the Attorneys were relieved of their duties. The finding of Justice WALTER is repeated (R. 98): "The other two actions have not yet been tried and are still pending undetermined."

D. Alleged excessiveness of the lien and unjustified reflection on the Supreme Court.

Although the Trustees unsuccessfully urged, both in the Appellate Division and the Court of Appeals, that the amount of the liens fixed by the Supreme Court were excessive, they attempt in this Court, through unsupported statements, to create the impression that the Supreme Court did not consider pertinent evidence brought to its attention and fixed the lien at an unconscionably high amount. This was done with the obvious purpose to influence this Court by the amounts of the liens fixed. It constitutes an unwarranted reflection upon the State Court. Under the circumstances it is essential to expose the misstatements and to summarize the record evidence upon which the liens were fixed.

FIRST: The following assertions in the Trustees' brief are without any record evidence to support them: that the judgments in Action No. 1 were settled for $150,000 against the principal defendants "because the defendants had no assets which would enable collection of a larger amount"

(p. 6); that the State Court fixed the lien at $100,000 "although the total collection by the estate on settlements of the action with all solvent defendants is approximately $190,000" (p. 10); that the Supreme Court, which fixed the lien, "knew that only $34,522 had been collected on account of the judgment in the New York action, and that the prospects were that not more than $150,000 would be collectible."

According to the record (R. 14-15), judgments in Action No. 1 were rendered against ten defendants in the following amounts:

A. Clarence K. Reynolds and William F. Woodward, jointly and severally	$1,180,185.53
B. William F. Woodward, individually	1,225.00
C. Jerome C. Brady, George H. Clayton, Vincent E. Ferretti and Calmur & Co., jointly and severally	1,310,109.13
D. Franklin Mayer	1,088,670.23
E. Prentice & Brady, partnership	40,886.18
F. William D. Boehn	11,538.98
G. George K. Hyslop	3,914.82

The settlement of $150,000 referred to by the Trustees, which took place after the Attorneys were relieved of their duties, related solely to defendants Clarence K. Reynolds and William F. Woodward. Not a word is mentioned in the record of any settlement with the other eight defendants or their solvency.

SECOND: The Trustees assert (Br. 25) that the State Court in fixing the lien "did not request the production" of certain pertinent papers relating to the above mentioned settlement with two of the defendants, thus insinuating that the Court did not properly consider evidence which the Trustees desired to introduce. It comes with bad grace from the Trustees to make this observation in view of the following facts: After the Attorneys com-

menced the New York lien proceedings by service of a petition upon the Trustees (R. 10 *et seq.*), it was arranged between the parties that the answer would be limited for the time being to the jurisdictional objection so that the Court could dispose of that issue first; and the answer interposed by the Trustees expressly alleges (R. 31) that they and the Attorneys "have agreed that only facts bearing on the jurisdiction of the Court be submitted at this time". The jurisdictional issue having been overruled, the State Court granted the Trustees ten days' time to answer on the merits (R. 109), that is, to March 6, 1942, which was extended to March 20, 1942 (R. 5), and set the matter down for hearing on March 31, 1942. On the day fixed for the hearing the Trustees appeared in court by Mr. Gerdes and, in spite of the fact that the order of the Bankruptcy Court authorized the lien proceedings in New York reserving merely the right in the Trustees to raise a jurisdictional question, which was done, they refused to proceed on the merits (R. 72, 73). The Court advised the Trustees, citing decisions of this Court, that they would not waive their right to review the jurisdictional question by going forward on the merits (R. 73, 110-111). At the conclusion of the first hearing the Court adjourned the case and requested the Attorneys to advise the Trustees of the adjournment "for the express purpose of giving them an opportunity to come in and present anything further that they desire—or present anything that they desire and, particularly to advise them that I would appreciate hearing from the Trustees their opinion as to the value of the services" (R. 85). The Trustees rejected this request and sent the letter (R. 93-4), referred to in their brief (p. 25), which concluded: "This letter is not intended as an appearance in the hearing before you, but as a friendly response—outside of the record—to your courteous request" (R. 94). Moreover, the reorganized corporation, the beneficiary of the Attorneys' services, condoned the action of the Trustees in refusing to participate

in the hearing and to furnish relevant evidence (R. 86-7, 91-3). Justice WALTER quite properly held that this letter delivered under such circumstances must be treated for judicial purposes as non-existent, stating (R. 9): "It is a strange notion that a litigant may deliberately refrain from attending a hearing before a court and yet convey allegedly pertinent ideas and information by means of a letter to the Judge."

THIRD: The Trustees' assertion that the amount of the lien as fixed was excessive and "represents more than 58% of the net recovery" (Br. 26) is absolutely false. The State Court's decision—reached after detailed proof was taken—was based upon the following essential facts:

1. The services of the Attorneys covered a period upwards of three years from 1938 to 1941, during which 8,814¼ hours of necessary time was devoted to Action No. 1, for which no compensation whatsoever had been received.

2. The Attorneys were highly successful in the litigation and obtained the substantial judgments referred to above. $187,000 has already been collected against only three of the ten defendants.

3. In the Virginia action, commenced by the Trustees against Richard S. Reynolds and his son, involving in part the identical transactions as those in Action No. 1, a stipulation was entered into whereby all of the evidence and proof adduced in the successful New York action, which consumed six weeks of trial, 4,800 pages of testimony and 448 exhibits, could be introduced into evidence in the Virginia Court. There was evidence that Richard S. Reynolds was receiving $100,000 a year as president of Reynolds Metals Company, and that his assets available for settlement of a lawsuit did not exceed $600,000 (R. 81).

Justice WALTER, before whom Action No. 1 was tried, and who was thoroughly conversant with the work, extent and value of the services rendered, stated that apart from the question of collectibility of judgments he would have no hesitation in fixing the lien in Action No. 1 at $145,000 or even a higher sum (R. 112). Nevertheless he did take into account the collectibility factor and substantially reduced the amount of the lien to $100,000 in Action No. 1 (R. 112, 113). It should be pointed out that in view of the fact that the Attorneys herein were not permitted to collect the judgments, but were relieved of their duties prior threto, Justice WALTER would have been justified in ignoring the collectibility of the judgments and computing the value of the services solely on the other factors. This, under the well-established rule that compensation for services of an attorney whose duties have been terminated must be fixed on a *quantum meruit* basis and cannot be made dependent on how successful some other attorney may be in collecting the judgment. *Martucci* v. *Brooklyn Children's Aid Society*, 284 N. Y. 408; *Matter of Tillman*, 259 N. Y. 133; *Matter of Krooks*, 257 N. Y. 329; *Matter of Weitling*, 266 N. Y. 184; *Matter of Montgomery*, 272 N. Y. 323.

The attempt of the Trustees to raise now the question of reasonableness by resort to incorrect statements outside the record will not impress this Court.

E. Alleged purpose and effect of stipulation and order of the Bankruptcy Court authorizing State lien proceedings.

Referring to the stipulation and order (R. 24-26) of Judge FAKE, authorizing the lien proceedings, the Trustees state (p. 6) that they withdrew their motion in the Bankruptcy Court to compel the Attorneys to turn over their papers so that the Trustees might request the State Court to recognize the exclusive jurisdiction of the Bankruptcy Court. That the Trustees should withdraw a proceeding already commenced in the Bankruptcy Court for the purpose of requesting a State Court, where no lien proceeding had as yet been commenced, to recognize the jurisdiction of

the Bankruptcy Court, is not only a transparent pretext but is contrary to the letter and purpose of the stipulation and order. A most casual examination of that document will demonstrate this (R. 24-6). This stipulation and order specifically directed the institution of the lien proceedings in the State Court with the permissive right in the Trustees, not a mandatory obligation imposed by the Bankruptcy Court, to raise a jurisdictional objection. Justice WALTER, properly construing this order, stated that the Bankruptcy Court "thus in effect authorized this proceeding subject to the trustees' claim of lack of jurisdiction" (R. 99).

It should be noted further that the Attorneys were "ordered" to institute the New York lien proceedings and not "permitted" as the Trustees state (Br. 7).

To say that this stipulation and order was simply an attempt to obtain from the State Court, as comity, a recognition of the exclusive jurisdiction of the Bankruptcy Court is absurd.

F. Alleged error in the record.

The Trustees' assertion (p. 9) that the opinion certified by the Court of Appeals is erroneous in stating that the appeal was upon constitutional grounds is groundless. The record plainly shows (R. 117), and the Trustees concede (Br. 9), that they appealed on constitutional grounds. This Court will not question the authenticity of the opinion so certified in the record merely because in the advance sheets the State reporter erroneously failed to state that the appeal was on constitutional grounds as well as by permission. Furthermore, the opinion of the Court of Appeals clearly shows that the Federal questions were the sole and decisive factors upon which the decision of that Court rested.

III

Answering the Trustees' legal contentions.

A

No contract arises from the plan of reorganization.

The first three points of the Trustees' brief are all predicated upon assumptions of fact contrary to the record and findings below.

Justice WALTER found, (a) that there is nothing in the plan, promulgated one and a half years after Action No. 1 was instituted and consummated two years thereafter, purporting to impair or destroy the lien rights of the Attorneys which attached at the commencement of the action, and (b) that the Attorneys were never parties to the plan of reorganization or the order confirming it. Such findings were affirmed by the Appellate Division and were not disturbed by the Court of Appeals, which based its decision on its construction of the Bankruptcy Act. The Trustees' legal arguments, therefore, are without basis of fact.

The Trustees, in their brief (pp. 12-13), seek to have this Court pass upon this factual issue and refer to two provisions in the plan (R. 52) which they contend embody the alleged contract by the Attorneys to waive their Attorneys' lien under Section 475: first, the provision that the Trustees shall retain continuing jurisdiction of the New York claims and shall continue to prosecute them, and that the bankruptcy court will fix reasonable compensation of the Trustees and their attorneys or counsel; and second, the provision which the Trustees have incorrectly quoted, reading as follows: "If the value of the portfolio of the Company shall, at any time prior to a complete and final adjudication on the merits of all of the claims reserved to the Trustees, be $300,000 or less, the assets of the Company shall not be further depleted by purchases or redemptions of debentures or shares of preferred stock without order of the Court after a hearing upon notice to the Trustees."

The first of these provisions has been referred to in our main brief (p. 47). The Trustees admit (p. 12n) that these terms of the plan are required by the Bankruptcy Act; and in fact the plan merely incorporates such provisions and goes no further. Obviously, the provisions of Chapter X providing that the bankruptcy court may fix the compensation of attorneys for the trustees, just as Section 62(d), the correlative section applicable to straight bankruptcy, are concerned only with allowances paid from assets of the estate in the possession of the bankrupcty court. It is significant that in *Sherman* v. *Buckley* and *In re Prudence Company*, discussed in our main brief (pp. 18-23), the Circuit Court of Appeals did not imply from such provisions an agreement of waiver by the Attorneys of their rights under Section 475.

As to the second provision in the plan referred to by the Trustees: Since the prosecution of the pending claims by the Debtor was vested in the Trustees under the Bankruptcy Act (Sec. 216 [13]) and the plan of reorganization, this provision constituted an obligation by the reorganized company to the Trustees not to exhaust its assets below a certain amount, so that the Trustees would be in a position effectually to prosecute all pending claims and to pay the expenses in connection therewith. It will be observed that the plan of reorganization contemplated a liquidation program, and this provision was inserted merely to insure that the Trustees would not be deprived of the necessary means to press the claims. This provision cannot be construed as a waiver by the Attorneys of their lien rights upon the New York actions.

The Discharge of the Attorneys Terminated Any Alleged Agreement Had There Been One

In addition to our contention that there never was an agreement as alleged by the Trustees, and that the Attorneys were not parties to the order confirming the plan, there is a third answer to the Trustees' contention given

by Justice WALTER; namely, that "if there be any ground for saying that any act by petitioners [Attorneys] constituted an implied agreement by them to look to the bankruptcy court for an allowance for their services in the actions in this court, as distinguished from an allowance for services rendered in the bankruptcy proceeding itself, such implied agreement was cancelled and terminated when the Trustees discharged them" (R. 109).*

In order to avoid the finding of fact that the Attorneys were discharged, the Trustees assert in their brief (pp. 15-16) that the Attorneys' contract was not abrogated by a wrongful discharge, and that the Court of Appeals held that the Attorneys had been permitted fully to perform the services for which they had been employed. The statement that there was no *wrongful* discharge is misleading, as no claim is made that the discharge was "wrongful". No one disputes that a client can discharge his attorney at any time for good reason, or as here, for no reason (see *Matter of Krooks*, 257 N. Y. 329, 331). The claim is, however, that the discharge terminated any agreement that may have existed and gave the Attorneys the immediate right to have their liens fixed under Section 475.

The assertion that the Attorneys were permitted to complete their services necessarily invites the inquiry as to what were the terms of the Attorneys' retainer. There was no express agreement setting forth the duration of their tenure. The only agreement alleged in the petition (R. 12) and found by the lower court (R. 98) arises from the order authorizing the Debtor and its Trustees to institute suits and to retain the Attorneys to act as their counsel. When attorneys are retained for a party bringing suit, it is implied that the attorneys will prosecute the action to judgment, and equally important, that they will take the necessary steps to collect the judgment, for that is the only purpose of the suit. *Larkin* v. *Frazier*, 224 N. Y. 421 (1918); *Ohlquist* v. *Nordstrom*, 143 Misc. 502, *aff'd* 238 N. Y. App. Div. 766, *aff'd* 262 N. Y. 696

* This point is referred to in our main brief (pp. 48-9).

(1933); 7 *Corpus Juris Secundum*, §96, p. 914; §116, pp. 947-8.

The implied agreement between the Attorneys and the Trustees is tersely summed up by Judge CHASE in the Court of Appeals in *Larkin* v. *Frazier, supra:*

> "Under the general authority conferred upon the defendant he was authorized to prosecute the action commenced by him for Clara C. Larkin to final judgment and to enforce collection thereof by the issuance of an execution thereon, to receive the avails of the execution from the sheriff and also to acknowledge satisfaction of the judgment at any time within the statutory period (citing cases). Likewise he would be authorized to institute proceedings supplemental to execution on the judgment. (*Ward* v. *Roy*, 69 N. Y. 96.) • • •"

In the instant case the Attorneys were notified (R. 22-3) that they were not to be permitted to collect the judgments in Action No. 1, but were to cease to function at the conclusion of the hearings before the Referee and that the Trustees themselves would handle the collection of the judgments. Moreover, the Attorneys were prevented from taking any further steps in connection with the *Globe* action and Action No. 2, pending untried. That the Attorneys, therefore, did not complete the services for which they were engaged, and were discharged is clear. Surely the Trustees and the Bankruptcy Court would have strenuously protested had the Attorneys on their own motion quit at that point and demanded payment for completed services.

The Trustees did not even deny or challenge the allegation in the petition of the Attorneys that they had been discharged (R. 20). Justice WALTER found that such was the fact, and this finding was unanimously affirmed by the Appellate Division. The Court of Appeals, whose jurisdiction as we have shown (*supra*, p. 4) is limited to the review solely of questions of law, could not and did not purport to alter this finding. The statement in the

opinion of the Court of Appeals, referred to by the Trustees (Br. 15), was not intended by that Court to reverse a finding made by both Courts below. It was merely an attempt by way of *obiter* to distinguish *Sherman* v. *Buckley*, which the dissenting judges of the Court of Appeals held placed jurisdiction in the State Court to fix the liens.

It is thus clear the Attorneys were bound by no contract constituting a waiver of their liens, and therefore that no question of *res judicata* or collateral attack of a Federal order is involved here.

On the foregoing analysis, *Stoll* v. *Gottlieb*, 305 U. S. 165, cited by the Trustees (p. 19) for the proposition that the order of the Reorganization Court may not be attacked collaterally is beside the point.

By tearing from its context one sentence in *Matter of Heinscheimer*, 214 N. Y. 361, the Trustees (Br. 16-17) urge that the charging lien under Section 475 of the Judiciary Law does not arise unless it was understood that the Attorneys were to share in the fruits of the recovery. The law is definitely to the contrary. The lien applies in all cases unless there is an express agreement of waiver, and the Courts will not make the assertion of the lien dependent upon any alleged claim that the Attorneys have other adequate protection. The Court of Appeals, in construing Section 475 specifically stated in *Robinson* v. *Rogers*, 237 N. Y. 467, 472, that

> "The statute has provided a lien in all cases and not merely where the client fails to provide some other form of security or protection, and the courts cannot themselves substitute another form of protection for that provided in the statute."

Nor is the *Heinscheimer* case inconsistent with the rule thus expressed. There the Court of Appeals actually enforced the charging lien to the extent of the value of the services rendered in connection with the particular action;

and as to other services performed under a general retainer unrelated to litigation, it properly held that no charging lien under the statute attached.

The Trustees have made the gratuitous and unsupported assertion (p. 9) that whether the Attorneys "have a lien for their services is not a matter of great importance to them in this case", and that they are amply protected without such lien. Suffice it to say that the Attorneys instituted the lien proceedings not as a futile gesture but because they deemed it essential that they have the protection granted them under Section 475; and any alleged security suggested by the Trustees cannot deprive them of a lien which the Court of Appeals has unequivocally held applies "in all cases".

B

The provisions of the Bankruptcy Act do not preclude the assertion and enforcement by the Attorneys of their liens under Section 475 of the Judiciary Law.

We have shown in considerable detail (Main Br. Point IV) that none of the applicable provisions of the Bankruptcy Act, examined in the light of their legislative history and judicial construction, reveals a congressional intent to preclude the state court from fixing liens upon causes of action prosecuted there by the direction of the bankruptcy court.

It will be seen that both the statutes and cases cited by the Trustees to support the contrary position are irrelevant. Not one of them involves the question of the right of an attorney to have the state court fix his lien upon suits prosecuted by him in that court with the authority of the bankruptcy court. They relate to applications for allowances made in the bankruptcy court out of funds in its possession or to services rendered in that court in the administration of the estate. Thus, in *Watkins* v. *Sedberry*, 261 U. S. 571; *In re Evans*, 117 Fed. 574; *In re McKenna*,

137 Fed. 611; *In re J. M. Fiske*, 209 Fed. 982; *In re Cheney*, 300 Fed. 465; *In re Levinson*, 19 F. (2d) 253, and *Watters* v. *Hamilton Gas Co.*, 29 F. Supp. 436, cited by the Trustees (pp. 22, 24-5), the Attorneys completed their services, collected funds for the estate and then applied to the bankruptcy court for compensation. The issue of State liens was not presented.

In referring to *Page* v. *Rogers*, 211 U. S. 575, the Trustees (p. 22) purported to paraphrase and quote this Court as holding

> "that 'the proper place to raise' the question as to the amount to be paid to the attorney for a bankruptcy trustee for services in a separate equity action was 'in the Bankruptcy Court' and not in the equity court."

This is a strange perversion of the opinion. The services were not rendered in a separate equity court, but, as this Court expressly stated, "this suit was brought in the bankruptcy Court itself" (p. 581). The decision, therefore, quite properly held that the fee should be fixed by the bankruptcy court where the suit was brought.

There is no magic in the language quoted from *In re Stemper*, 222 Fed. 690, referred to by the Trustees (p. 23) to the effect that an attorney for a bankrupt trustee may not acquire uncontrolled rights in the bankrupt's assets. The quotation becomes understandable when read in the light of the fact that the attorney was claiming a lien by virtue of an agreement with the trustee and not a state statute. Moreover, in this very quotation the rule is stated to apply to compensation for services which the Attorney "claims shall be paid out of the trust estate."

Fanning v. *Poe*, 76 F. (2d) 707, cited by the Trustees (pp. 20-21) as an authority "on all fours" is distinguishable on a number of grounds. There, an attempt was made by an attorney for a Georgia state court receiver to have the bankruptcy court in another jurisdiction fix and determine his lien under the Georgia law on claims of the receiver prosecuted in the bankruptcy court. In the first

place, the bankruptcy court is one of limited jurisdiction, having statutory authority concerned with the administration of a bankrupt estate. There is no provision in the Bankruptcy Act for the creation of attorneys' liens and the enforcement and determination thereof in the bankruptcy court. In the case at bar, on the other hand, Section 475 of the Judiciary Law creates attorneys' liens and provides for the enforcement thereof in the Court in which the action was instituted. In the second place, in the *Fanning* case, the Court expressly pointed out that no consent was obtained from the receivership court to institute the lien proceedings in the bankruptcy court; whereas, in the instant case, the lien proceedings in New York were expressly directed by order of the Bankruptcy Court. Finally, the *Fanning* decision was rendered by the Fifth Circuit prior to the *Sherman, Cup Craft* and *Ohio Oil* decisions handed down by the Second and Eighth Circuit Courts. Insofar as it may be said to contain any contrary dictum, it is not entitled to any weight in view of the later holdings.

The Trustees (p. 21) purport to quote from Section 62-d of the Bankruptcy Act and then omit an important qualifying clause without indicating such omission. Their version is as follows:

> "or any other attorney, seeking compensation for services rendered by him in a proceeding, shall file with the court a petition setting forth the value and extent of services rendered, the amount requested and what allowances, if any, have theretofore been made to him."

Actually that portion of the section quoted reads as follows:

> "or any other attorney, seeking compensation for services rendered by him in a proceeding *under this Act or in connection with such proceeding,* shall file with the court a petition, etc." (Emphasis supplied.)

The phrase so opportunely omitted indicates clearly, as the Attorneys claim (Main Br., pp. 41-2) that Section 62 relates to allowances for services rendered within the bankruptcy court itself or from funds in its possession.

The other sections of the Bankruptcy Act cited by the Trustees (pp. 23-4) likewise apply to such cases and do not purport to affect State attorneys' liens upon causes of action and proceeds thereof within the jurisdiction of the State Court.

In order to illustrate their claim that the reorganization court should have exclusive jurisdiction, the Trustees present a biased and incorrect picture as to the method of the State Court in fixing the fee. This attempt based upon statements outside the record has been fully answered (*supra*, pp. 6 *et seq.*). Such attempt was hardly fair coming from Trustees who rejected the request of the State Court Justice that they furnish him with all pertinent information respecting the proposed fees and the status of the debtor without prejudice to their claim that the State Court was without jurisdiction (R. 72-3, 85-6, 91-3, 95, 110-11).

The Trustees attempt (Br., Point VIII) to distinguish *Sherman* v. *Buckley* and the other persuasive decisions. A number of the alleged distinctions have already been anticipated and refuted (Main Br., Points I and II; p. 21n).

The other claimed distinctions are without substance:

(a) The Trustees state (p. 48) that in the *Sherman* case there was a substitution of the attorneys, whereas in the instant case there was no substitution or application for substitution. We have shown (*supra*, p. 5) that this statement is contrary to the record facts and findings below.

(b) Likewise, the contention (p. 49) that the Attorneys were not discharged is at variance with the facts (*supra*, pp. 13-6).

(c) The Trustees further urge that the lien of the Attorneys in the *Sherman* case arose prior to bankruptcy and was perfected thereafter as expressly permitted by Section 67-b of the Bankruptcy Act; whereas the liens herein arose after the bankruptcy proceedings and do not come within the purview of that section. The *Sherman* case had nothing whatever to do with Section 67-b, and not a single reference is made to this provision either in the briefs or in the decision. Under Section 67 all liens against the property of a bankrupt obtained within four months prior to bankruptcy proceedings and at a date when insolvency existed are void, with the exception of the liens of creditors specifically enumerated in subdivision b of that section. The attorneys in the *Sherman* case commenced suit years prior to the bankruptcy proceedings and their lien under Section 475 of the Judiciary Law arose from the moment suit was instituted. Consequently, Section 67, relating to liens arising within the four-month period, has no application to the case.

C

The enforcement of the lien by the State Court violates no rule against securing or enforcing a lien upon assets of a debtor during reorganization.

The Trustees urge (Points V and VI) that the determination of the Attorneys' lien by the State Court contravened the rule that no lien "on assets of a debtor" can be secured during the pendency of a reorganization proceeding, and that no State Court, without the consent of the reorganization court, may enforce a lien against assets of the debtor during such proceedings.

There are three conclusive answers:

First: There is and can be no asset within the custody of the bankruptcy court until the causes of action are realized upon through suit in the State Court. (See *In re Borok*, 50 F. [2d] 75, 77 [C. C. A. 2] and *In re Worrall*, 79 F. [2d] 88, 90, 91 [C. C. A. 2].) Since, as we have

shown, the laws of New York have imposed as a condition of access to its courts that the attorney shall have a charging lien to be fixed by that Court—which in effect constitutes an equitable assignment *pro tanto* of the cause of action—it necessarily follows, as Justice WALTER pointed out (R. 106), that "it is only the part [of the cause of action] which so remained vested in the bankrupt client which ever became subject to administration in bankruptcy". This is in accord with the statement of Judge SWAN in *In re Prudence Company*, 96 F. (2d) 157, *cert. den.* 305 U. S. 616, that "Success having been achieved, they [the Trustees] can reap the benefit of the judgment, but they take it subject to the attorneys' charging lien".

It is thus apparent that reference by the Trustees to provisions in the Bankruptcy Act and to decisions relating to mortgage foreclosures and receiverships or other lien proceedings affecting real or personal property which admittedly come within the custody of the bankruptcy court have no bearing whatever upon causes of action in favor of the debtor.

SECOND: The provisions of the Bankruptcy Act referred to by the Trustees, prohibiting the obtaining or enforcing of liens against the property of the bankrupt or debtor, obviously refer to liens arising out of claims, contracts or proceedings against the bankrupt or debtor which antedated the bankruptcy. The cases cited by the Trustees (pp. 28, 29, 33) are instances of this nature. They do not purport to cover the situation at bar, where the liens were fixed for services rendered to the Debtor and the Trustees subsequent to the institution of the bankruptcy proceedings. Thus, in *Van Huffel* v. *Harkelrode*, 284 U. S. 225, the lien according to the opinion of Mr. Justice BRANDEIS was "for unpaid state taxes which had accrued prior to bankruptcy". Moreover, upon sale of the property the lien was transferred to the purchase price (p. 226). *New York* v. *Irving Trust Company*, 288 U. S. 329, likewise involved a State's claim for additional franchise taxes for the years 1919 to 1928 against a corporation which was adjudged a

bankrupt in March of 1929. *Isaacs* v. *Hobbs Tie & Timber*, 282 U. S. 734, involved a mortgage given as security for a note issued prior to the bankruptcy proceedings. In *Straton* v. *New*, 283 U. S. 318, the claim of the creditor arose prior to bankruptcy; his judgment having been obtained in April, 1927, and the voluntary petition in bankruptcy having been filed on October 11, 1928. Indeed, in the *Straton* case, this Court refused to enjoin the State proceedings to sell the real estate which had been commenced more than four months prior to the bankruptcy.

THIRD: The bald, unsupported statement of the Trustees (p. 28) that a lien cannot be secured against assets of a bankrupt or debtor during the pendency of bankruptcy or reorganization proceedings is flatly at variance with the decisions that a debtor and its trustees coming into a State Court are subject to State lien laws. An excellent example is *Boteler* v. *Ingels*, 308 U. S. 57. There the trustee in bankruptcy had been operating the debtor's trucking business. He claimed that he was not liable to pay penalties under the California Motor Vehicle Tax Law and that the vehicles were not subject to the statutory lien covering the tax and penalties thereon. Upon the trustee's petition the District Court ordered the License Commissioner to issue licenses, directed that the vehicles be sold ex lien and permitted California to file a claim for fees, without penalties, within thirty days, failing which the claim was to be barred. The Circuit Court of Appeals reversed, ordering in the alternative that the fees and penalties be paid or that the vehicles be disposed of subject to the lien of the State for unpaid taxes and penalties. This Court affirmed the order of the Circuit Court of Appeals and rejected the contention of the trustee that he was immune from the local tax laws.

The Trustees can draw no comfort from *In re Fonda, Johnstown & Gloversville Railroad Co.*, 126 F. (2d) 604, cited in their brief (p. 28). No question of the right to enforce a State lien arose. As a matter of fact, in repudi-

ating the trustee's claim that he was immune from the particular tax and in directing him to pay it, the Circuit Court cited the *Boteler* case and reiterated the rule that Trustees are subject to, not immune from, State law.

United States v. *Wood*, 290 Fed. 109, *aff'd* 263 U. S. 680, cited by the Trustees (p. 28), also was not concerned with the enforcement of local liens arising during reorganization proceedings. It involved an attempt of the creditor to enforce a claim against the bankrupt upon funds in the hands of the trustee in bankruptcy.

In sum, the contention of the Trustee that no lien can be secured against assets during the reorganization proceeding, if correct, would necessarily mean that trustees may carry on business or conduct suits in a State Court with entire disregard of all State lien laws. It can hardly be contended, in view of the *Boteler* and like authorities, that a reorganization trustee of a trucking company, who, subsequent to his appointment, delivers cars to be repaired or stored by a garageman, is immune from a local garageman's or artisan's lien. Nor a trustee of a building company from a mechanic's lien. An attorney's lien is equally valid.

D

The Bankruptcy Court conferred jurisdiction upon the State Court to fix the liens upon the New York causes of action through its direction that such actions be instituted in the State Court. Moreover, the Bankruptcy Court, under Section 77-b, never had jurisdiction of Action No. 1.

The Trustees (Br., Point VII) contend that the Bankruptcy Court never granted jurisdiction to the State Court to fix the liens, and further that it had no power to waive or delegate its jurisdiction to fix fees of its agents.

There are two bases, as we have shown in our main brief, for the jurisdiction of the State Court to fix the liens upon the causes of action:

(1) Assuming that the Bankruptcy Court initially had jurisdiction of the cause of action, it relinquished jurisdiction to the State Court over the cause of action and all incidents thereof, including the fixing and enforcement of the Attorneys' lien by authorizing the institution of suit there (Main Br., Point I).

(2) Under Section 77-b in effect when Action No. 1 was instituted, the bankruptcy court never had jurisdiction over such cause of action (see *In re Borok* and *In re Worrall, supra,* p. 21); such jurisdiction was vested solely and exclusively in the State Court, the only forum where the Trustees could enforce the claim (Main Br., Point III).

Entirely avoiding the second of these bases which, in our opinion, is irrefutable, the Trustees endeavor to challenge the validity of the first ground by asserting that while the Bankruptcy Court conferred upon the State Court power to determine the issues in the New York suits this did not carry with it jurisdiction to fix the liens, since a lien proceeding constitutes "a separate and independent proceeding". This is clearly untenable. It is well settled that a proceeding to fix an attorneys' lien upon a cause of action is substantively an incident of the main suit, not a separate and independent proceeding. Indeed, as Justice WALTER stated (R. 104):

> "a proceeding to fix the lien is so strictly ancillary to that suit that federal jurisdiction of such a proceeding exists even though there be no such diversity of citizenship between the parties to such proceeding as would support federal jurisdiction of the fixation proceeding apart from the court's jurisdiction over the client's suit—and that, too, even though no substitution of attorneys in the client's suit is asked (*Woodbury* v. *Jergens Co.*, 69 Fed. 2d 49; *Lawrence* v. *Commodore Nav. Corp'n, supra,* [27 F. supp. 139])."

Clearly, the substantive rights of an attorney to the enforcement of his lien under Section 475, as defined in the *Sherman* and other decisions discussed in our main

brief, are not dependent upon whether the procedural method of asserting the lien is by motion in the action or by special proceeding. *Peri* v. *New York Central R. R.*, 152 N. Y. 521, referred to by the Trustees (pp. 38-9), merely stated, as Justice WALTER pointed out (R. 101-2), that lien proceedings are separate proceedings "in a procedural sense". In fact, supplementary proceedings to collect a judgment recovered in an action are regarded under the New York law in a procedural sense as a separate proceeding requiring new process, etc., but it cannot be denied that it is substantively an incident of the main suit and has no independent existence.

The argument of the Trustees that the Federal Court has no power to waive or delegate its jurisdiction to fix fees is of no moment here. It applies only to cases such as *Wright* v. *City National Bank and Trust Co.*, 104 F. (2d) 285, cited by the Trustees (p. 40), which relate to allowances for services rendered within the confines of the bankruptcy court, or to cases such as *U. S. Fidelity and Guaranty Co.* v. *Bray*, 225 U. S. 205, referred to by the Trustees (p. 40), which is concerned with the distribution of assets in the custody of the bankruptcy court.

PART TWO

ANSWERING THE SECURITIES AND EXCHANGE COMMISSION, *AMICUS CURIAE*

All of the arguments advanced in the brief of the Securities and Exchange Commission are found in substance in the brief of the Trustees and have already been refuted.

It should be noted that the Securities and Exchange Commission, as the Trustees, has significantly left unanswered the rule that a trustee coming into a State Court is in the same position as any other litigant, and the decisions of this Court in *Boteler* v. *Ingels* and *Palmer* v. *Massachusetts,* that debtors and bankrupt trustees are not immune from the operation of state laws.

Also, the Commission, just as the Trustees, has not addressed itself to the issue at hand—the power of a State Court to determine and enforce a lien upon a judgment and proceeds thereof obtained in a suit prosecuted in its court with the authority of the Bankruptcy Court (see pp. 2-3, *supra*).

No force can be found in the assertion of the Commission (p. 14) that "Section 475 is not * * * a normal procedure by which attorneys obtain their compensation for conducting litigation". It is quite true that attorneys in the normal course of events do not face the necessity of availing themselves of the protection granted by Section 475. It should be emphasized, however, that the situation at bar does not fall within the category of the normal and ordinary course of events. The Attorneys here had carried on with success an important litigation on behalf of the Debtor and later its Trustees with the approval of the Bankruptcy Court; they handled the main action for a period of upwards of three years, during two and a half years of which they represented the present Trustees; they conducted a thorough and painstaking investigation of the

complicated facts and complex questions of law, an inkling of which can be gleaned from the Court's decision in Action No. 1 (reported in 28 N. Y. Supp. (2d) 622-667); they handled intermediate appeals to the Court of Appeals; they conducted the six-weeks trial of Action No. 1 and were successful in their claims against all the important defendants; they conducted hearings before the referee which resulted in very substantial judgments. When they had traveled this long course and were ready to reap the fruits of their efforts by entering judgments and collecting them, the Trustees, without any cause for discharge or even notice or opportunity to the Attorneys to be heard before any tribunal, terminated their services and demanded the turnover of all papers. That is certainly not the normal procedure between attorney and client. Accordingly, the Attorneys were advised to take the appropriate means, perhaps not normal in ordinary situations, but assuredly normal and necessary in the circumstances at bar, to protect themselves.

Nor does the Commission advance its argument by asserting (p. 15) that Section 475 is "narrower than the allowance provisions of the Bankruptcy Act", that "it cannot be used where the action involved does not result in a recovery"; and that "if attorneys appointed by a bankruptcy court are unsuccessful in a state court action to recover a money judgment * * * they have no alternative but to resort to the Bankruptcy Court for allowances". These statements are undoubtedly correct. The fact is, however, that fortunately in the case at bar, the Attorneys were successful in the State Court action in recovering a money judgment, and consequently come four-square within the scope, however narrow, of the protective provisions of this Section.

Argument I of the Commission

The attempt is made by reference to various provisions of the Bankruptcy Act to spell out a congressional intent to abrogate state attorneys' lien laws in all actions insti-

tuted by attorneys in a State Court on behalf of a debtor or bankruptcy trustee. Such attempt has been refuted in our main brief (Point IV) and *supra*, pages 17 *et seq.*

The Commission stresses the various safeguards contained in the Bankruptcy Act, such as the necessity of filing affidavits under Chapter X to insure the highest standards of fiduciary conduct on the part of the attorneys and to protect the assets of the estate. The clear inference sought to be created is that there are insufficient safeguards in a hearing before the State Court. This is an unjustified reflection upon the state processes. A lien proceeding in the State Court conforms with well accepted concepts of due process; it involves a judicial hearing, and ample notice and opportunity to be heard. The Trustees as the duly constituted representatives of the security holders are permitted to introduce any evidence whatever bearing upon the validity or extent of the lien. Judge WALTER in the instant case, who sat in the trial of Action No. 1 and therefore had first-hand knowledge of the services performed, not only welcomed such proof but repeatedly requested the Trustees to present anything that they desired bearing upon the merits of the lien. The State Court was also in a position to judge whether the Attorneys had complied with the highest standards of undivided loyalty. There is not a suggestion in the record that they had not. In fact, since it appears that the Attorneys represented the principal debenture and preferred stockholders' committee, they were required to file the affidavits under Sections 210 and 211 of Chapter X revealing the pertinent facts bearing upon their status. Finally, as we have shown in our main brief (p. 43) where a trustee sues in a state court, the defendant may plead and prove a counterclaim in the state court and the determination of such counterclaim is just as binding upon the Trustee and the estate as if it had been heard and allowed by a bankruptcy referee upon notice to all interested parties. The efficacy of such determination has never been questioned on the ground that the safeguards in the bankruptcy proceedings were more comprehensive or better than those in the state court.

Argument II of the Commission

This contention that the Bankruptcy Court has not surrendered its exclusive jurisdiction to determine fees, has already been fully answered.

The power of the State Court herein to fix the liens upon the New York actions and proceeds thereof, as distinguished from an alleged power to fix fees in general, stems (1) from the order of the Bankruptcy Court authorizing the institution of the suits in the State Court, (2) from the Federal Court's order and stipulation that the lien proceedings be forthwith instituted, and (3) from the provisions of Section 77B under which the State Court and not the bankruptcy court was the only tribunal that had jurisdiction of Action No. 1.*

Argument III of the Commission

The position advanced by the Commission that the attorneys waived their New York attorneys' liens, has been thoroughly refuted.

The import of the argument advanced is that in every instance that an attorney represents a trustee or debtor in a state court, he waives all local attorneys' lien rights. This is contrary to all of the adjudicated cases. Such drastic change requires a clear legislative expression:—none exists.

The Commission urges that the reorganization statutes formed part of the retainer of the Attorneys. We do not quarrel with this assertion. We claim, however, that the statutes do not purport to operate as a waiver by attorneys of their local liens or to confer immunity upon debtors and trustees from state laws applicable to all litigants.

* The Commission (p. 8) assumes that Chapter X is applicable to Action No. 1 by virtue of Section 276-c of that Chapter. As we have shown (Main Br. pp. 27-28) the provisions of Chapter X while applicable to prior proceedings in the reorganization court, do not apply to prior plenary actions instituted in another court. See *In re Standard Gas & Electric Company*, 119 F. (2d) 658, 663 (C. C. A. 3); *Tilton* v. *Model Taxi Corp.*, 113 F. (2d) 86, 88.

The order of the Court of Appeals should be reversed and the orders of the Supreme Court affirmed by the Appellate Division should be reinstated.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1943.

No. 183.

B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler, and Murray MacElhinny, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

—against—

John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

On Petition for Writ of Certiorari to the Court of Appeals of the State of New York.

BRIEF OF REORGANIZATION TRUSTEES IN OPPOSITION TO PETITION.

JOHN GERDES,
JAMES D. CARPENTER, JR.,
As Trustees of Reynolds Investing Company, Inc., Debtor, Pro Se, Respondents.

John Gerdes,
Mary-Chase Clark,
Of Counsel.

August 31, 1943.

The Court Press, N. Y. C.

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Respondents.

On Petition for Writ of Certiorari to the Court of Appeals of the State of New York.

BRIEF OF REORGANIZATION TRUSTEES IN OPPOSITION TO PETITION.

Opinions Below.

The opinions of the state Supreme Court appear on pages 98 to 113 of the record and are not officially reported. The Appellate Division wrote no opinion. The

opinion of the state Court of Appeals and dissent appear on pages 124 to 129 of the record, and are reported in 290 N. Y. 468.

Statutes Involved.

The provisions of the Bankruptcy Act and other federal and state statutes involved, are set forth in the Appendix to this brief.

Outline of Case.

This Court is asked to review the refusal of the New York court to fix the compensation to be paid to attorneys appointed by a federal district court in a reorganization proceeding under the Bankruptcy Act to bring and prosecute suits in a state court upon causes of action constituting assets of the estate of the debtor.

The reorganization Trustees, under authority conferred by the federal reorganization court, opposed the fixing of the Attorneys' fee by the state court on the following grounds:

1. The Attorneys had entered into an express and implied contract that the amount of their fee would be fixed by the federal reorganization court.

2. Even if there had been no contract binding the Attorneys to the fixation of their fee by the federal reorganization court, such court has exclusive jurisdiction over the fixing of allowances to attorneys appointed by it to prosecute, in behalf of debtors in possession or trustees,

causes of action which are assets of the estate of the debtor.

3. The Attorneys are bound by the plan of reorganization—approved, confirmed and consummated with their active approval and consent—which expressly provides that their fee is to be fixed by the federal reorganization court. The plan, and order confirming it, are *res judicata;* they cannot be attacked collaterally in a state court.

The state Court of Appeals held:

1. That the Attorneys had bound themselves by contract to permit the federal reorganization court to fix the value of their services; and

2. That even if there were no contract to that effect, the federal reorganization court had exclusive jurisdiction, under the Federal Constitution, the Bankruptcy Act, and other federal statutes, to fix the reasonable value of the services of attorneys appointed by it to assist in the administration of an estate in reorganization proceedings under the Bankruptcy Act.

As its decision on the two foregoing matters determined the issues, the state Court of Appeals did not pass upon the question as to whether the plan of reorganization and the order confirming it could be attacked collaterally in a state court.

Facts.

A petition for the reorganization under Section 77B of the Bankruptcy Act of Reynolds Investing Company, Inc. (hereinafter called the Debtor) was filed on May 18, 1938, in the United States District Court for the District of New Jersey (R. 11). The petition was approved, and the Trustees were appointed on January 19, 1939 (R. 12), under the provisions of Chapter X of the Bankruptcy Act (Chandler Act) which had become applicable to the proceeding on September 22, 1938 (Bankruptcy Act, section 276c(1)).

After jurisdiction had been conferred on it by the filing of the petition, the reorganization court made an order (dated August 1, 1938) appointing the Attorneys, as attorneys for the Debtor, to institute and prosecute in the New York courts certain claims in favor of the Debtor against its former officers, directors and others (R. 12). Action in the New York court was started August 4, 1938 (R. 12). After their appointment, the Trustees, by order dated February 10, 1939, were substituted as parties plaintiff in place of the Debtor (R. 12).

In November 1939 the Attorneys, who were also the attorneys for the two most important creditor and stockholder committees in the reorganization proceeding,* approved the plan of reorganization proposed by the Trustees and urged the Court, creditors, stockholders, and other interested parties, to approve and accept the plan (R. 30). The plan so approved expressly provided that the federal reorganization court retained jurisdiction

* The Attorneys received $36,000 in allowances from the reorganization court for their services as attorneys for these committees (R. 26).

to "fix the reasonable compensation" to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of" the claims being prosecuted in the New York court by the Attorneys (R. 29).

Some changes were made in the plan originally proposed by the Trustees in October 1939 and approved by the Attorneys in November 1939, but no change was ever requested or made in the provisions which reserved to the federal reorganization court jurisdiction over the determination of the value of the Attorneys' services. The plan of reorganization, which was confirmed (R. 31) by the court by order dated June 17, 1940, and fully consummated* in 1940 (R. 30), contained the same reservation of jurisdiction of the federal organization court over the fixing of the compensation of the Attorneys for their services in the state court (R. 52).

The Attorneys performed most of the services for which they seek compensation *after* they had approved the plan, and after the plan had been confirmed and consummated. They prepared for trial, conducted a six weeks trial in the New York court during the early part of 1941, conducted hearings before a state court referee in the summer of 1941, and entered judgment in favor of the Trustees in the state court in November 1941 (R. 14, 15).

In June 1941 the Trustees, under authority from the federal reorganization court, notified the Attorneys that after the Attorneys completed the reference then pending and entered judgment in the action, their services for

* The proceeding was terminated, except for the reserved jurisdiction of the reorganization court and the Trustees over the claims being prosecuted by the Attorneys, and other unsettled or unadjusted claims of the Debtor and its estate, as required by Section 216(13) of the Bankruptcy Act.

the Trustees were to discontinue (R. 22, 23). No other attorneys were substituted in the New York action for the Attorneys. The Trustees did not appear *pro se* therein. They settled for $150,000 the judgments entered by the Attorneys in favor of the Trustees in the New York action against the principal defendants (because the defendants had no assets which would enable collection of a larger amount) with the approval of the federal reorganization court after hearings upon notice to the Attorneys, the Securities and Exchange Commission, all creditors and stockholders, and other parties in interest. This sum of $150,000 is being held in escrow for the satisfaction of such claim as the Attorneys may finally establish in either the state or federal court.

The Trustees made a motion in the federal court to compel the Attorneys to deliver to the Trustees the papers and exhibits in the New York actions. The Attorneys contested the jurisdiction of the federal court and asserted that the New York court had exclusive jurisdiction.

Following the suggestion of this Court in *Gross* v. *Irving Trust Co.*, 289 U. S. 342, at page 345 (that the federal court might well instruct its trustee in bankruptcy "to request the state court to recognize the exclusive jurisdiction of the" federal court "before taking final action"), the Trustees, with the consent of the federal court, withdrew their motion in the federal court under a written stipulation (R. 24-26) which permitted the Attorneys to present the questions to the state court, with an express reservation of the right of the Trustees to question the jurisdiction of the state court (R. 26).

A proceeding was brought by the Attorneys in the state court to fix the value of their services and to enforce a lien for such amount. The lower state court

fixed $100,000 as the value of such services, and added $2,250 for interest from November 27, 1941 to April 15, 1942, the date of the entry of its order (R. 7). When it fixed these amounts the state court knew that a proceeding was pending before the federal court to settle for $450,000 the judgments against the principal defendants (R. 93).

The state Appellate Division affirmed the lower court, without opinion. The state Court of Appeals reversed, and dismissed the proceeding.

After instituting the principal action in the New York court, and after the appointment of the Trustees under Chapter X, the Attorneys were authorized to bring two additional actions in behalf of the Trustees in the New York court: the action designated as Action No. 2, and the action designated as the Globe Action.

There was no substitution of attorneys or of the Trustees *pro se*, and no application for such substitution, in Action No. 2. The action—which involved some of the defendants who were defendants in Action No. 1—was settled in conjunction with the settlement of Action No. 1. The aforesaid sum of $150,000 is also held in escrow for the protection of any claim which may be established by the Attorneys for services in Action No. 2. The allowance by the lower state court for such services was $2000.

The Globe action has been abandoned. Neither the Attorneys nor the Trustees believe that there is a reasonable prospect of recovery. No substitution or application for substitution of attorneys or of the Trustees *pro se* has been made. Nothing has been done in the action since the Attorneys discontinued their services. The fund of $150,000 is also held for the satisfaction of any

claim which may be established by the Attorneys for their services in this action.' The allowance to the Attorneys by the lower state court for their services was $750.

Error in the Record.

An important error appears in the record on page 124. It is stated, as part of the official report of the opinion of the Court of Appeals, that the appeal to the Court of Appeals was "on constitutional grounds from an order of the Appellate Division". The correct statement, as found in the official reports, *Matter of Brown (Gerdes)*, 290 N. Y. 468, is: "Appeal, by permission of the Court of Appeals, from an order of the Appellate Division."

The New York practice permits appeals to the Court of Appeals as of right (on constitutional questions), or by permission of the Appellate Division or the Court of Appeals (in which case the Court of Appeals is not restricted to the consideration of constitutional questions).

The Trustees appealed both as of right and with the permission of the Court of Appeals. The Court considered local state questions of law as well as constitutional questions.

Trustees' Position and Summary of Argument.

(1) As to questions of local state law:

The state court disposed of the claim of the attorneys, as a matter of local state law, by holding (a) that the Attorneys had agreed that their compensation would be

fixed by the federal reorganization court and (b) that this contract had not been abrogated by any wrongful discharge of the Attorneys before the completion of their services. The federal questions are moot.

(2) As to questions of federal law:

(a) The federal question of jurisdiction is moot because the Attorneys are bound by the plan of reorganization and the order confirming it, both of which provide that the federal court shall fix the fee of the Attorneys. The federal court order and plan are *res judicata* and cannot be attacked collaterally in a state court.

(b) The state court correctly held that the federal court has exclusive jurisdiction even if no contract or plan expressly gives it such jurisdiction.

(c) There is no conflict between the decision of the state court herein and applicable decisions of this and other federal courts.

POINT I.

The questions of local state law are determinative of the issues. The federal questions are moot.

In their brief, the Attorneys ignore completely the primary issue in this case. The primary issue is not as to whether a state court may enforce a lien for services rendered by attorneys in a state court action, but whether the state court, in determining the amount for which a lien, if any, shall be enforced, *must* disregard the con-

tract of the Attorneys under which they agreed that the amount of their compensation would be fixed by the federal reorganization court.

The Attorneys do not require a lien to insure payment of their fee. The assets are ample, and the plan makes adequate provision for such payment. What the Attorneys desire is that the state court disregard their contract and determine the amount of their claim as though there were no contract.

Section 475 of the New York Judiciary Law gives a lien only in an amount determined as provided in the contract of the attorneys. Section 474 of the New York Judiciary Law provides: "The compensation of any attorney or counsellor for his services is governed by agreement, express or implied, which is not restrained by law," except where the contract is made by the attorney with the guardian of an infant.

The Attorneys herein agreed to the fixation of their compensation by the federal reorganization court.

The plan of reorganization provides (R. 52):

> "All claims in favor of the Debtor or of the Debtor's estate not settled or adjusted in the reorganization proceedings, or in the plan, or in connection with the consummation of the plan, shall be retained and enforced by the Trustees. * * *

> "The Court will retain continuing jurisdiction over such claims and the prosecution thereof * * * The Court will from time to time fix the reasonable com-

* These provisions are required by sections 216(13) and 221(4) of the Bankruptcy Act.

pensation to be paid to the Trustees, *and their attorneys or counsel*, for services in the prosecution of such claims, * * *"*

The Attorneys approved the plan as early as November, 1939, and urged the creditors and stockholders represented by them to approve and accept it (R. 30).** The plan was confirmed by order dated June 17, 1940, and was consummated in 1940, with the active support of the Attorneys (R. 30).**

As the Attorneys approved the provisions of the plan, under which it was specified that their fees would be fixed by the federal court, before they conducted the trial of the New York action or performed the most important part of their services, the condition that their fee be fixed by the federal court was a part of their contract with the Trustees and the federal court. The state Court of Appeals so held (R. 128):

> "It is unnecessary to consider whether it was within the power of the [reorganization] court to surrender this jurisdiction, since it would appear that both as a matter of law and as a matter of fact the retainer of these attorneys was subject to the condition that the amount of any fees would be fixed by the United States District Court."

In addition, when the Attorneys accepted appointment by the federal court, the statutory provisions requiring the federal court to fix their fees became, by implication,

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* These provisions are required by sections 216(13) and 221(4) of the Bankruptcy Act.

** These allegations in paragraphs 11 and 12 of the Trustees' answer were expressly admitted in the reply of the Attorneys (R. 68).

a part of their contract. In its opinion the New York Court of Appeals said (R. 126):

> "Also, since these attorneys were appointed by the court in this reorganization proceeding and nothing was said as to fees, the services of the attorneys were undertaken subject to all the provisions of the Bankruptcy Act with respect to the compensation for such services. * * * Under such circumstances, even if no exclusive jurisdiction had been given to the Federal Court, the attorneys would in the normal course return to have their compensation fixed by the court by whom their appointment had been made."

In the state court the Attorneys conceded that if there were no wrongful discharge of the Attorneys by the Trustees, the state court would have no jurisdiction to fix their compensation. But they contended that under the state law they had been wrongfully discharged by the Trustees, and that such discharge abrogated their contract that the federal reorganization court was to fix their compensation, and gave jurisdiction to the state court.

The precise position taken by the Attorneys is shown by the following quotation from pages 7 and 8 of their brief on their motion for a reargument in the state Court of Appeals:

"POINT I.

IN STATING AND ASSUMING THAT RESPONDENTS HAD FULLY PERFORMED THEIR SERVICES, THE MAJORITY OF THIS COURT MISAPPREHENDED AND OVERLOOKED THE RECORD FACTS AND THE FINDINGS OF BOTH COURTS BELOW, AND THEREBY MISCONCEIVED THE FUNDAMENTAL ISSUE

ON THIS APPEAL AND THE DIRECT APPLICABILITY OF *Sherman* v. *Buckley* UPON WHICH THE MINORITY OF THIS COURT RELIED.

"Judge Finch, in the prevailing opinion, states that respondents fully performed the services for which they were retained. On that assumption he deems the issue presented on this appeal to be whether the New York Court had the power to grant an allowance to respondents for such completed services, and concludes that exclusive jurisdiction resided in the Bankruptcy Court. The facts as found by both courts below, however, are that respondents were discharged prior to the full performance of their services, that the actions which they were retained to prosecute were not completed and that appellants sought to substitute themselves in place of respondents in the pending New York actions.

"The issue on this appeal, therefore, is not whether the State Court has jurisdiction to grant allowances in general to attorneys appointed by the Bankruptcy Court after services have been completed by such attorneys. On that proposition there is no dispute; where an attorney appointed by a Bankruptcy Court has completed his work, the fixing of his compensation and the granting of allowances are made by the Bankruptcy Court and all the provisions of the Bankruptcy Act referred to by Judge Finch, relating to allowances to attorneys in the Bankruptcy Court, become effective.

"The issue before this Court is as follows:

"Where a company in bankruptcy, and its trustees, with the approval and by the direction of the Bankruptcy Court, retain New York attorneys and commence suits in the courts of that State to enforce claims of the bankrupt estate, and the Trustees thereafter discharge the attorneys before they have completed their services or seek to substitute them

selves, *pro se* or others as their attorneys, does the New York Court have jurisdiction *in rem* to fix the lien of the discharged attorneys upon the causes of action in New York and the proceeds thereof?

"Thus the question whether respondents were in fact discharged is fundamental."

The Court of Appeals reaffirmed, by denying the motion for reargument, its finding that, as a matter of local state law, the Attorneys had not been wrongfully discharged, but had been permitted fully to perform the services for which they had been employed. The Court said (R. 128):

"* * * the attorneys herein were permitted fully to perform the services for which they were appointed, namely to reduce the claims to judgment. * * *".

The state Court of Appeals held, as a matter of state law, that the Attorneys were bound by contract to have their fee fixed by the federal court. It also held, as a matter of state law, that the contract had not been abrogated by a wrongful discharge of the Attorneys. The federal jurisdictional question is therefore moot and not decisive.

POINT II.

The federal question of jurisdiction is moot because the Attorneys are bound by the plan of reorganization and the order confirming it, both of which provide that the Federal Court shall fix the fee of the Attorneys. The Federal Court order and plan are *res judicata* and cannot be attacked collaterally in a state court.

The plan of reorganization provides that the federal reorganization court retains jurisdiction to "fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of" the claims prosecuted by these Attorneys (R. 52).

The plan also provides only for the payment of claims of creditors which have been proved in the proceedings and for the payment of such reorganization debts and expenses as are allowed by the federal reorganization court (R. 37, 55).

The order confirming the plan of reorganization provides that costs and expenses of administration shall be paid only if approved by the reorganization judge after a hearing upon proper notice under the Bankruptcy Act (R. 66).

The Attorneys are bound by the foregoing provisions of the plan and of the order confirming the plan. They were parties to the reorganization proceeding. They participated in the formulation of the plan and order of confirmation. They urged the court and the security

holders' committees represented by them to approve and accept the plan and the order confirming it. Their time to appeal has long since expired.

Even if the federal reorganization court had acted beyond its power in confirming a plan containing these provisions—as was not the case—the Attorneys are bound by the plan and the order which confirmed it, which are *res judicata* as to them. They cannot attack the plan or order collaterally in a state court. *Stoll* v. *Gottlieb*, 305 U. S. 165.

POINT III.

The state court correctly held that the federal court has exclusive jurisdiction even if no contract or plan expressly gives it such jurisdiction.

In addition to holding that the Attorneys were bound under applicable state law by the terms of their contract, which provided for the fixing of their fees by the federal reorganization court, the Court of Appeals held that the federal reorganization court would have had exclusive jurisdiction to fix the fees of the Attorneys even if there had been no contract binding them to such fixation. In so holding, the state court merely followed the clear mandate of the Bankruptcy Act, the Federal Judicial Code, and the decisions of this Court and other federal courts.

It would be extremely difficult to improve upon the learned statement on this point of Judge Finch in the opinion of the New York Court of Appeals (R. 125-129):

"[fol. 191] It is submitted that the Federal court in

a reorganization proceeding has exclusive jurisdiction to award fees to attorneys appointed by it in payment of services to the bankrupt estate in the collection of claims in a State court. The Congress has power to make uniform laws upon the subject of bankruptcy. (U. S. Const., art. I, §8, clause IV.) In the National Bankruptcy Act the Congress has set up a comprehensive system of bankruptcy administration and conferred exclusive jurisdiction upon the Federal courts. Chapter 10 of the Act (Bankruptcy Act, §§111, 114), under which this reorganization proceeding expressly confers upon the United States District Court 'exclusive jurisdiction of the debtor and its property wherever located'. This is reenforced by the specific provision that State courts shall have no jurisdiction over bankruptcy matters. (Federal Judicial Code, §256; see, also, *Gross* v. *Irving Trust Co.*, 289 U. S. 342, *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478.) Not only does chapter 10 specifically confer exclusive jurisdiction of the debtor and its property upon the Federal court, but in addition there is specifically given exclusive jurisdiction to determine costs, expenses and reasonable compensation for services rendered in reorganization proceedings (Bankruptcy Act, §§62, 241-250), and there are set forth numerous meticulous provisions designed to make effective the control of the Federal court over fees and expenses. Allowances under chapter 10 may be made only after a hearing upon notice to the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate (§247). No longer are allowances fixed in a hearing confined solely to the attorneys in interest, but under chapter 10 interested parties enjoy the statutory right to appear and be heard (§206 [U. S. Code, tit. 11, §606]). In addition, attorneys

seeking compensation must file a statement under oath showing whether they have acquired or transferred claims against or stock of the debtor after the commencement of the proceeding, and no compensation can be allowed to any attorney who, after assuming to act in that capacity, has purchased or sold claims or stock of the debtor (§249). Also an attorney seeking compensation must by affidavit inform the Federal court whether he has made any agreement with any person for a division of his compensation (§62). If allowances and fees could be awarded in the State courts, all these elaborate provisions for a notice and hearing to all the parties interested, and prohibition against attorneys dealing in claims against the estate of the debtor could be evaded, and fees in as many State courts as there were assets of the debtor which should be collected therein, would be fixed without regard to the amount of the total expenses and assets as a whole, since the State court is dealing only with particular claims and cannot have adequate knowledge of what will comprise the entire estate [fol. 192] as to assets and total costs, expenses and fees. * * *

"The control provided by the Bankruptcy Act over costs and expenses of administration, particularly including fees and allowances, is an important part of the entire reorganization and bankruptcy system. The system aims to provide maximum protection and relief for embarrassed or insolvent debtors consistent with protection and fairness to creditors and security holders. If the system is to work with satisfaction, there must be a proper balance giving on the one hand fair remuneration to those who administer the system, and on the other hand a limitation upon the total cost of administration, so that the Act in operation does not become too expensive. Centralized control over expenses incident to reorganization in bankruptcy to supplant State and Federal equity proce-

dures, so as to reduce the cost of corporate reorganization, was one of the forces making for the enactment of the reorganization and bankruptcy statutes. (*Callaghan* v. *Reconstruction Finance Corp.*, 297 U. S. 464.) The importance of this centralized control over expenses incident to reorganization is seen in the provision of the Act (§258 [U. S. Code, tit. 11, §658]) providing that administration allowances for services rendered in State or Federal court proceedings, later supplanted by a reorganization proceeding, must be determined not in the court supervising the prior proceeding but in the reorganization court. (*Matter of Keystone Realty Holding Co.*, 117 F. (2d) 1003.)

"The Bankruptcy Act and chapter 10 show congressional intent to treat a reorganization proceeding not as ordinary litigation between private parties, but as involving rights and interests of many members of the general public who are usually unrepresented or inadequately represented in the proceeding. As the Supreme Court of the United States has indicated, these statutory provisions are de- [fol. 193] signed to facilitate the participation of these various interests in matters in which they have a vital concern, and in any event furnish, so far as possible, safeguards for their protection. (*Securities & Exchange Commission* v. *U. S. Realty & Improvement Co.*, 310 U. S. 434.)"

POINT IV.

There is no conflict between the decision of the state court herein and applicable decisions of this and other federal courts.

It has uniformly been held that attorneys appointed by courts to bring suits in other courts to recover on claims should look to the appointing courts for the fixation of their compensation:

Watkins v. *Sedberry*, 261 U. S. 571, 575;
Page v. *Rogers*, 211 U. S. 575, 581;
Fanning v. *Pope*, 76 F. (2d) 707, 709;
In re Stemper, 222 Fed. 690, 692;
Davidson v. *Friedman*, 140 Fed. 853.

In numerous cases attorneys have applied to bankruptcy or reorganization courts to fix their fees for prosecuting actions in state courts,* but diligent research has failed to reveal even one case in which a state court has attempted to fix the amount to be paid for services of attorneys appointed in a bankruptcy or reorganization proceeding to conduct litigation in behalf of the estate in a state court.

All the cases cited on this point by the Attorneys involved actions on claims arising before the bankruptcy or reorganization. None of them involved the fixing of the fees of attorneys for services rendered upon appointment

* See *In re Evans*, 117 Fed. 574; *In re McKenna*, 137 Fed. 611; *In re J. M. Fiske*, 269 Fed. 982; *In re Cheney*, 300 Fed. 465; *In re Levinson*, 19 F. (2d) 253; *Watters* v. *Hamilton Gas Co.*, 29 F. Supp 436, 477 (¶71, 72-3).

by a bankruptcy or reorganization court. None involved a debt or expense of administration governed by section 62 and 241 of the Bankruptcy Act.

The facts in *Sherman* v. *Buckley*, 119 F. (2d) 280, and *New York Creditmen's Assn.* v. *Schlesinger*, 126 F. (2d) 472, differ from the facts in this case in the following respects: the attorneys were not appointed by the bankruptcy court; their services were rendered to bankrupts *before* the bankruptcy proceedings were initiated; their claims were not debts or expenses of administration; the attorneys had contingent contracts and were not permitted to prosecute the claims to judgment—they were wrongfully discharged. (*New York Creditmen's Assn.* v. *Schlesinger* is the case referred to in the state court as *Cup Craft Paper Corp.* v. *Federal Paper Board Co.*)

The New York Court of Appeals distinguished the foregoing cases from the case herein, as follows (R. 128, 129):

> "Respondents rely upon the cases of *Sherman* v. *Buckley* (119 F. 2d 280, cert. den., 314 U. S. 657) and *Cup Craft Paper Corp.* v. *Federal Paper Board Co.* (262 App. Div. 91, appeal dismissed, 288 N. Y. 529). In both of these cases the attorneys were not appointed by the Bankruptcy Court, but were retained and their services were rendered to the bankrupts and the liens arose, before the bankruptcy. While it is true that in *Sherman* v. *Buckley* (*supra*) the attorney continued as an attorney of record after the bankruptcy, there is nothing in the record to show that any services were rendered by him after the bankruptcy and before the substitution of attorneys, and no claim was made by him for services after the initiation of the bankruptcy proceeding. In addition, the attorneys in both of these cases were discharged

and not permitted to complete the services for which they had been employed under a single contract of contingent retainer, whereas the attorneys herein were permitted fully to perform the services for which they were appointed, namely to reduce the claims to judgment. Also in the *Sherman* and *Cup Craft* cases the claims for services were provable as debts of the bankrupt and were not within the statutory provisions regulating allowances for services in the administration of a reorganization or bankruptcy estate. As already noted, in the case at bar the attorneys were appointed by the court pending the reorganization proceeding to perform services as [fol. 194] agents and appointees of the court. The allowances for the attorneys were administration expenses covered by the allowance provisions of the Bankruptcy Act."

In *In re Prudence Co.*, 96 F. (2d) 157, the attorney had been employed by the debtor before the initiation of the reorganization proceeding. His services were not performed under appointment by the reorganization court. Nevertheless, although not a debt or expense of administration, the attorney made *application to the reorganization court* for the allowance of his claim!

The other cases cited by the Attorneys in Point I (Petitioners' Brief, pp. 1 to 6) involved claims by outside persons against bankrupts and debtors, or their property, which arose before the initiation of the bankruptcy or reorganization proceedings. None involved debts or expenses of administration.

The contention that the federal reorganization court waived its jurisdiction, is without merit. The New York Court of Appeals stated as to this contention (pp. 127, 128):

> "If we are correct in holding that the jurisdiction of the Federal court to determine these fees is exclusive, then it would seem clear that no waiver by the Federal court under the circumstances in the case at bar has been attempted."

In any event, the jurisdiction of the federal district court over such matters of administration as the fixing of fees for services in connection with the administration of the estate, cannot be delegated. See *U. S. Fidelity & Guaranty Co.* v. *Bray*, 225 U. S. 205, 217, 218; *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 739; *Gross* v. *Irving Trust Co.*, 289 U. S. 342, 344.

Section 241 of the Bankruptcy Act expressly puts upon the reorganization judge the duty of fixing the fees of attorneys appointed by him to assist the trustees in the administration of the estate. It is the discretion of the district judge—not the discretion of any other person or tribunal—which the statute demands. The district judge cannot avoid this obligation by delegation to another court. He cannot even delegate it, under a plan, to the trustees or committees in the proceedings (*Wright* v. *City National Bank & Trust Co.*, 104 F. (2d) 285).

Even if the reorganization judge had power to delegate this important administrative function, he could, at most, delegate only his own power. He could not evade the clear mandate of statute and court rule by delegating the matter to another court free from the restrictions imposed upon him by Sections 62, 206, 247 and 249 of the

Bankruptcy Act and General Order in Bankruptcy 44. The requirements of these statutes and rules were not met in the proceeding in the state court.

The cases on the proposition that a governmental agency which submits a controversy to a court for determination is bound by the judgment therein, do not apply. The controversy submitted by the Trustees to the jurisdiction of the state court in the action against the Reynolds officers and directors had nothing to do with the controversy between the Attorneys and the Trustees as to which court should fix the fees of the Attorneys. The Trustees are bound by the judgment in the *Reynolds* action, but that judgment did not cover the fees of the Attorneys—and could not cover such fees (only statutory costs in favor of the Trustees could be, and were, included). The proceeding of the Attorneys for the fixation of their fees was an entirely separate proceeding, with different parties, and involving different issues. *Peri* v. *New York Central Rr.*, 152 N. Y. 521, 526.

The cases, such as *Foust* v. *Munson S. S. Lines*, 299 U. S. 77, cited by the Attorneys in Point II (Petitioners' Brief, p. 7), dealing with an abuse of discretion in a lower federal court in refusing permission to litigate issues in a state court, are not relevant because: (1) they all relate to claims against a bankrupt or debtor or against its property arising before the bankruptcy or reorganization proceeding—they were not debts or expenses of administration; and (2) in each case it was a higher federal court which reviewed such discretion—no case holds that a state court may take jurisdiction without permission of the federal court.

The cases cited by the Attorneys in Point III (Petitioners' Brief, pp. 8 to 12), dealing with the difference in jurisdiction, under Section 23 of the Bankruptcy Act, of a court in proceedings under Section 77B and Chapter X, are clearly not in point. Section 23 does not deal with proceedings for the allowance of administration expenses but with the institution of separate plenary suits brought by trustees in bankruptcy against outside parties on claims which arose in favor of the bankrupt before the institution of the bankruptcy proceeding. In any event, Chapter X was applicable to the controversy between the Attorneys and the Trustees, because such controversy arose in 1941—more than three years after the provisions of Chapter X applied "in their entirety" to this reorganization proceeding (Section 276c(1) of the Bankruptcy Act).*

The Trustees request that the petition for a writ of certiorari be denied.

JOHN GERDES,
JAMES D. CARPENTER, JR.,
As Trustees of Reynolds Investing Company, Inc., Debtor, Pro Se, Respondents.

JOHN GERDES,
MARY-CHASE CLARK,
Of Counsel.

August 31, 1943.

* The petition in the reorganization proceeding was not approved until January 19, 1939, after Chapter X took effect on September 22, 1938.

APPENDIX.

Constitution and Statutes.

State Statutes.

NEW YORK JUDICIARY LAW, SECTIONS 474 AND 475.

§474. *Compensation of attorney or counsellor.*

The compensation of an attorney or counsellor for his services is governed by agreement, express or implied, which is not restrained by law, * * *

§475. *Attorney's lien in action, special or other proceeding.*

From the commencement of an action, special or other proceeding in any court or before any state or federal department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien.

Federal Constitution.

ARTICLE I, SECTION 8, CLAUSE 4.

The Congress shall have Power To establish * * * and uniform Laws on the subject of Bankruptcies throughout the United States;

Federal Statutes.

JUDICIAL CODE, SECTION 256
(28 U. S. C. A. 371).

Exclusive jurisdiction of United States courts. The jurisdiction vested in the courts of the United States in the cases and proceedings hereinafter mentioned, shall be exclusive of the courts of the several States: * * *

Sixth. Of all matters and proceedings in bankruptcy.

FEDERAL BANKRUPTCY ACT.

SEC. 23. JURISDICTION OF UNITED STATES AND STATE COURTS.—a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67, and 70 of this Act.

SEC. 62. EXPENSES OF ADMINISTERING ESTATES; UNAUTHORIZED SHARING OF FEES; WITHHOLDING ALLOWANCES. a. The actual and necessary costs and expenses incurred by officers in the administration of estates shall, except

where other provisions are made for their payment, be reported in detail, under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred. * * *

c. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, rendering services in a proceeding under this Act or in connection with such proceeding, shall not in any form or guise share or agree to share his compensation for such services with any person not contributing thereto, or share or agree to share in the compensation of any person rendering services in a proceeding under this Act or in connection with such proceeding, to which services he has not contributed: *Provided, however*, That an attorney-at-law may share such compensation with a law partner or with a forwarding attorney-at-law, and may share in the compensation of a law partner.

d. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, seeking compensation for services rendered by him in a proceeding under this Act or in connection with such proceeding, shall file with the court his petition setting forth the value and extent of the services rendered, the amount requested and what allowances, if any, have theretofore been made to him. Such petition shall be accompanied by his affidavit stating whether an agreement or understanding exists between the petitioner and any other person for a division of compensation and, if so, the nature and particulars thereof. If satisfied that the petitioner has, in any form or guise, shared or agreed to share his compensation or in the compensation of any other person contrary to the provisions of this subdivision, the court shall withhold all compensation from such petitioner.

Federal Bankruptcy Act.

Sec. 111. Where not inconsistent with the provisions of this chapter, the court in which a petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and its property, wherever located.

Sec. 114. Upon the approval of a petition, the jurisdiction, powers, and duties of the court and of its officers, where not inconsistent with the provisions of this chapter, shall be the same as in a bankruptcy proceeding upon adjudication.

Sec. 206. The debtor, the indenture trustees, and any creditor or stockholder of the debtor shall have the right to be heard on all matters arising in a proceeding under this chapter. * * *

Sec. 216. A plan of reorganization under this chapter— * * *

(13) may include provisions for the settlement or adjustment of claims belonging to the debtor or to the estate; and shall provide, as to such claims not settled or adjusted in the plan, for their retention and enforcement by the trustee or, if the debtor has been continued in possession, by an examiner appointed for that purpose; * * *

Sec. 221. The Judge Shall Confirm a Plan if Satisfied that— * * *

(4) all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge

and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge; * * *

SEC. 241. The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceeding under this chapter—

(1) by a referee;

(2) by a special master;

(3) by the trustee and other officers, and the attorneys for any of them;

(4) by the attorney for the debtor; and

(5) by the attorney for the petitioning creditors.

Such compensation of referees and trustees shall not be governed by sections 40 and 48 of this Act. * * *

SEC. 242. The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in connection with the administration of an estate in a proceeding under this chapter or in connection with a plan approved by the judge, whether or not accepted by creditors and stockholders or finally confirmed by the judge—

(1) by indenture trustees, depositaries, reorganization managers, and committees or representatives of creditors or stockholders;

(2) by any other parties in interest except the Securities and Exchange Commission; and

(3) by the attorneys or agents for any of the foregoing except the Securities and Exchange Commission.

SEC. 243.—The judge may allow reasonable compensation for services rendered and reimbursement for proper

costs and expenses incurred by creditors and stockholders, and the attorneys for any of them, in connection with the submission by them of suggestions for a plan or of proposals in the form of plans, or in connection with objections by them to the confirmation of a plan, or in connection with the administration of the estate. In fixing any such allowances, the judge shall give consideration only to the services which contributed to the plan confirmed or to the refusal of confirmation of a plan, or which were beneficial in the administration of the estate, and to the proper costs and expenses incidental thereto.

SEC. 244. Where a petition is filed under section 127 of this Act, the judge may allow, if not already allowed, reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in the pending bankruptcy proceeding—

(1) by a marshal, receiver, or trustee, as provided in subdivision g of section 48 of this Act, and the attorneys for any of them;

(2) by the attorney for the petitioning creditors;

(3) by the attorney for the bankrupt; and

(4) by any other persons and the attorneys for any of them entitled under this Act to compensation or reimbursement in such bankruptcy proceeding.

SEC. 245. Where a petition is filed in a pending bankruptcy proceeding, the judge may allow reasonable compensation for services rendered and the proper costs and expenses incurred in such bankruptcy proceeding by a referee in bankruptcy. In fixing such compensation, the judge shall not be restricted by the provisions of section 40 of this Act.

Federal Bankruptcy Act.

SEC. 246. Upon the dismissal of a proceeding under this chapter, or the entry of an order adjudging the debtor a bankrupt, the judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in such proceeding prior to such dismissal or order of adjudication by any persons entitled thereto, as provided in this chapter, and shall make provision for the payment thereof, and for the payment of all proper costs and expenses incurred by officers in such proceedings.

SEC. 247. The judge shall fix a time of hearing for the consideration of applications for allowances, of which hearing notice shall be given to the applicants, the trustee, the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate, except that, in the case of allowances for services and reimbursement in a superseded bankruptcy proceeding, notice need be given only to the applicants, the debtor, the trustee, and the unsecured creditors, and may be given to such other classes of creditors or other persons as the judge may designate. In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that bankruptcy be proceeded with, notice of the hearing to consider allowances need not be given to stockholders.

SEC. 248. In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that a superseded bankruptcy be proceeded with, the compensation allowed by the judge, in the course of the proceeding under this chapter, to the referee, marshal, receiver, or trustee in the bankruptcy proceeding for services rendered by them in such bankruptcy

proceeding shall be deemed to have been allowed in such bankruptcy proceeding, and such compensation shall be considered in connection with the making of future allowances therein or shall be readjusted, so as to comply with the provisions of this Act fixing their compensation in a bankruptcy proceeding.

SEC. 249. Any persons seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter, shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred.

SEC. 250. Appeals may be taken in matters of law or fact from orders making or refusing to make allowances of compensation or reimbursement, and may, in the manner and within the time provided for appeals by this Act [title], be taken to and allowed by the circuit court of appeals independently of other appeals in the proceeding, and shall be summarily heard upon the original papers.

SEC. 258. The judge shall make such provision as may be equitable for the protection of the obligations incurred by a receiver or trustee in such prior proceeding and

for the payment of the reasonable costs and expenses incurred therein as may be allowed by the judge.

SEC. 276 c. The provisions of sections 77A and 77B of chapter VIII, as amended, of the Act entitled "An Act to establish a uniform system of bankruptcy throughout the United States", approved July 1, 1898, shall continue in full force and effect with respect to proceedings pending under those sections upon the effective date of this amendatory Act, except that—

(1) if the petition in such proceedings was approved within three months prior to the effective date of this amendatory Act, the provisions of this chapter shall apply in their entirety to such proceedings;

General Orders in Bankruptcy.

Order 44.

APPOINTMENT OF ATTORNEYS.

No attorney for a receiver, trustee or debtor in possession shall be appointed except upon the order of the court, which shall be granted only upon the verified petition of the receiver, trustee or debtor in possession, stating the name of the counsel whom he wishes to employ, the reasons for his selection, the professional services he is to render, the necessity for employing counsel at all, and to the best of the petitioner's knowledge all of the attorney's connections with the bankrupt or debtor, the creditors or any other party in interest, and their respective attorneys. If satisfied that the attorney represents no interest adverse to the receiver, the trustee, or the estate in the matters upon which he is to be engaged, and that his employment would be to the best interests of the estate, the court may authorize his employment, and such employment shall be for specific purposes unless the court is satisfied that the case is one justifying a general retainer. If without disclosure any attorney acting for a receiver or trustee or debtor in possession shall have represented any interest adverse to the receiver, trustee, creditors or stockholders in any matter upon which he is employed for such receiver, trustee, or debtor in possession, the court may deny the allowance of any fee to such attorney, or the reimbursement of his expenses, or both, and may also deny any allowance to the receiver or trustee if it shall appear that he failed to make diligent inquiry into the connections of said attorney. * * *

FILE COPY

DEC 13 43

CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1943.

No. 183.

B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler, and Murray MacElhinny, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

—against—

John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

On Petition for Writ of Certiorari to the Court of Appeals of the State of New York.

BRIEF OF REORGANIZATION TRUSTEES.

JOHN GERDES,
JAMES D. CARPENTER, JR.,
As Trustees of Reynolds Investing Company, Inc., Debtor, Pro Se,
Respondents.

John Gerdes,
Mary-Chase Clark,
Of Counsel.

December 8, 1943.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1943.

No. 183.

B. H. Inness Brown, David Paine, Ethelbert Warfield, J. Fearon Brown, George Koegler, and Murray MacElhinny, individually and as co-partners under the firm name of Kellogg, Emery & Inness-Brown,

and

Lawrence S. Greenbaum, Edward S. Greenbaum, Herbert A. Wolff, Morris L. Ernst, Jonas J. Shapiro, Wallace D. Jennings, Samuel J. Schur and Alexander Lindey, individually and as co-partners under the firm name of Greenbaum, Wolff & Ernst,

Petitioners,

—against—

John Gerdes, and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor,

Respondents.

On Petition for Writ of Certiorari to the Court of Appeals of the State of New York.

BRIEF OF REORGANIZATION TRUSTEES.

Opinions Below.

The opinions of the state Supreme Court appear on pages 98 to 113 of the record and are not officially reported. The Appellate Division wrote no opinion. The opinion of the state Court of Appeals and dissent appear on pages 124 to 129 of the record, and are reported in 290 N. Y. 468.

Statutes Involved.

The provisions of the Bankruptcy Act and other federal and state statutes involved, are set forth in the Appendix to this brief.

Outline of Case.

This Court is asked to review the refusal of the New York court to fix the compensation to be paid to attorneys (hereinafter referred to as the "Attorneys") appointed by a federal district court in a reorganization proceeding under the Bankruptcy Act to bring and prosecute suits in a state court upon causes of action constituting assets of the estate of the debtor.

The reorganization trustees (hereinafter referred to as the "Trustees"), under authority conferred by the federal reorganization court, opposed the fixing of the Attorneys' fee by the state court on the following grounds:

1. The Attorneys have entered into an express or implied contract that the amount of their fee is to be fixed by the federal reorganization court.

2. Even if there were no contract binding the Attorneys to the fixation of their fee by the federal reorganization court, such court has exclusive jurisdiction over the fixing of allowances to attorneys appointed by it to prosecute, in behalf of debtors in possession or trustees, causes of action which are assets of the estate of the debtor.

3. Section 475 of the New York Judiciary Law does not grant a lien under circumstances such as exist in this situation. In any event, no lien may be secured against assets of a debtor during the pendency of a proceeding under Chapter X of the Bankruptcy Act.

4. No state court, without the consent of the reorganization court, may enforce a lien against assets of a debtor during the pendency of a proceeding under Chapter X of the Bankruptcy Act. Such consent was not given by the reorganization court or Trustees.

5. The Attorneys are bound by the plan of reorganization—approved, confirmed and consummated with their active approval and consent—which expressly provides that their fee is to be fixed by the federal reorganization court. The plan, and order confirming it, are *res judicata;* they cannot be attacked collaterally in a state court.

The state Court of Appeals held:

1. That the Attorneys have bound themselves by contract to permit the federal reorganization court to fix the value of their services; and

2. That even if there were no contract to that effect, the federal reorganization court has exclusive jurisdiction, under the Federal Constitution, the Bankruptcy Act, and other federal statutes, to fix the reasonable value of the services of attorneys appointed by it to assist in the administration of an estate in reorganization proceedings under the Bankruptcy Act.

As its decision on these matters determined the issues, the state Court of Appeals did not pass upon the other questions.

Facts.

A petition for the reorganization under Section 77B of the Bankruptcy Act of Reynolds Investing Company, Inc. (hereinafter called the Debtor) was filed on May 18, 1938, in the United States District Court for the District of New Jersey (R. 11). The petition was approved, and the Trustees were appointed on January 19, 1939 (R. 12), under the provisions of Chapter X of the Bankruptcy Act (Chandler Act) which had become applicable to the proceeding on September 22, 1938 (Bankruptcy Act, section 276c(1)).

After jurisdiction had been conferred on it by the filing of the petition, the reorganization court made an order (dated August 1, 1938) appointing the Attorneys, as attorneys for the Debtor, to institute and prosecute in the New York courts certain claims in favor of the Debtor against its former officers, directors and others (R. 12). Action in the New York court was started August 4, 1938 (R. 12). After their appointment, the Trustees, by order dated February 10, 1939, were substituted as parties plaintiff in place of the Debtor (R. 12).

In November 1939 the Attorneys, who were also the attorneys for the two most important creditor and stockholder committees in the reorganization proceeding,* ap-

* The Attorneys received $36,000 in allowances from the reorganization court for their services as attorneys for these committees (R. 28).

proved the plan of reorganization proposed by the Trustees and urged the Court, creditors, stockholders, and other interested parties, to approve and accept the plan (R. 30). The plan so approved expressly provides that the federal reorganization court retains jurisdiction to "fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of" the claims being prosecuted in the New York court by the Attorneys (R. 29).

Some changes were made in the plan originally proposed by the Trustees in October 1939 and approved by the Attorneys in November 1939, but no change was ever requested or made in the provisions which reserve to the federal reorganization court jurisdiction over the determination of the value of the Attorneys' services. The plan of reorganization, which was confirmed (R. 31) by the court by order dated June 17, 1940, and fully consummated* in 1940 (R. 30), contains the same reservation of jurisdiction of the federal reorganization court over the fixing of the compensation of the Attorneys for their services in the state court (R. 52).

The Attorneys performed most of the services for which they seek compensation *after* they had approved the plan, and after the plan had been confirmed and consummated. They prepared for trial, conducted a six weeks trial in the New York court during the early part of 1941, conducted hearings before a state court referee in the summer of 1941, and entered judgment in favor of

* The reorganization proceeding was terminated, except for the reserved jurisdiction of the reorganization court and the Trustees over the claims being prosecuted by the Attorneys, and other unsettled or unadjusted claims of the Debtor and its estate, as required by Section 216(13) of the Bankruptcy Act.

the Trustees in the state court in November 1941 (R. 14, 15).

In June 1941 the Trustees, under authority from the federal reorganization court, notified the Attorneys that after the Attorneys completed the reference then pending and entered judgment in the action, their services for the Trustees were to discontinue (R. 22, 23). No other attorneys were substituted in the New York action for the Attorneys. The Trustees did not appear *pro se* therein. The judgments entered by the Attorneys in favor of the Trustees in the New York action against the principal defendants, because the defendants had no assets which would enable collection of a larger amount, were settled for $150,000 with the approval of the federal reorganization court after hearings upon notice to the Attorneys, the Securities and Exchange Commission, all creditors and stockholders, and other parties in interest. This sum of $150,000 is being held in escrow for the protection of the Attorneys, pending the determination of this appeal.

The Trustees made a motion in the federal court to compel the Attorneys to deliver to the Trustees the papers and exhibits in the New York actions. The Attorneys contested the jurisdiction of the federal court and asserted that the New York court had exclusive jurisdiction.

Following the suggestion of this Court in *Gross* v. *Irving Trust Co.*, 289 U. S. 342, at page 345 (that the federal court might well instruct its trustee in bankruptcy "to request the state court to recognize the exclusive jurisdiction of the" federal court "before taking final action"), the Trustees, with the consent of the federal court, withdrew their motion in the federal court

under a written stipulation (R. 24-26) which permitted the Attorneys to present the questions to the state court, with an express reservation of the right of the Trustees to question the jurisdiction of the state court (R. 26).

After the foregoing state court action had been terminated by the entry of final judgment on November 5, 1941 (R. 15), a separate and independent proceeding was brought by the Attorneys in the state court (by petition dated December 22, 1941) to fix the value of the services rendered by them in the aforesaid action and in two other actions (hereinafter referred to as Action No. 2 and the Globe Action), and to enforce liens for such services.

The Trustees objected to the jurisdiction of the state court. The state court overruled the objections to its jurisdiction and fixed $100,000 as the value of the services rendered in the aforesaid action, adding $2,250 for interest from November 27, 1941 to April 15, 1942, the date of the entry of its order (R. 7). When it fixed these amounts the state court knew that a proceeding was pending before the federal court to settle for $150,000 the judgments against the principal defendants (R. 93, 94).

The order of the state court adjudged the Attorneys to have a lien for the aforesaid sum upon the judgment entered in the New York action against the old Reynolds directors and upon "the proceeds thereof in whatever hands they may come" (R. 7), and provided, further, that the Attorneys could apply to the said state court "for additional and further relief to enforce said lien" (R. 8).

On appeal, the state Appellate Division affirmed the lower court, without opinion. The state Court of Appeals reversed, and dismissed the proceeding.

After instituting the principal action in the New York court, and after the appointment of the Trustees under Chapter X, the Attorneys were authorized to bring two additional actions in behalf of the Trustees in the New York court: the action designated as Action No. 2, and the action designated as the Globe Action.

There was no substitution of attorneys or of the Trustees *pro se*, and no application for such substitution, in Action No. 2. The action—which involved some of the defendants who were defendants in Action No. 1—was settled in conjunction with the settlement of Action No. 1. The aforesaid sum of $150,000 is also held in escrow, pending the determination of this appeal, for the protection of the Attorneys for services in Action No. 2. The allowance by the lower state court for such services was $2000.

The Globe action has been abandoned. Neither the Attorneys nor the Trustees believe that there is a reasonable prospect of recovery. No substitution or application for substitution of attorneys or of the Trustees *pro se* has been made. Nothing has been done in the action since the Attorneys discontinued their services. The fund of $150,000 is also held in escrow, pending the determination of this appeal, for the satisfaction of any claim which may be established by the Attorneys for their services in this action. The allowance to the Attorneys by the lower state court for their services was $750.

Additional facts are set forth in the argument of the Points.

Error in the Record.

An important error appears in the record on page 124. It is stated, as part of the official report of the opinion of the Court of Appeals, that the appeal to the Court of Appeals was "on constitutional grounds from an order of the Appellate Division". The correct statement, as found in the official reports, *Matter of Brown (Gerdes)*, 290 N. Y. 468, is: "Appeal, by permission of the Court of Appeals, from an order of the Appellate Division."

The New York practice permits appeals to the Court of Appeals as of right (on constitutional questions), or by permission of the Appellate Division or the Court of Appeals (in which case the Court of Appeals is not restricted to the consideration of constitutional questions).

The Trustees appealed both as of right and with the permission of the Court of Appeals (R. 123). The Court considered local state questions of law as well as constitutional questions.

Position of the Trustees.

Whether the Attorneys have a lien for their services is not a matter of great importance to them in this case. There is no doubt that any claim which they may legally establish will be paid in full.

As stated by the Attorneys themselves in their petition in the lower state court (R. 19-20), the plan prepared by the Trustees and confirmed and consummated in the reorganization proceeding provides that "the [reorganized]

Company is compelled to keep available $300,000 of its assets to assure payment of expenses incurred in the prosecutions of these claims". In addition, the Trustees have voluntarily agreed to the holding of $150,000 in cash—proceeds of the settlement of the New York action—in escrow for the satisfaction of the Attorneys' claim.

The really important question to those interested in the Reynolds reorganization is whether the state court may fix the *amount* of compensation to be paid out of the reorganization estate to these Attorneys, appointed by the reorganization court, for services as Attorneys for the Trustees in the administration of assets of the reorganization estate. (The state court has fixed the compensation to the Attorneys at $100,000, plus $2250 interest and costs, although the total collection by the estate on settlements of the action with all solvent defendants is approximately $190,000.)

Other questions of general importance in the administration of estates under Chapter X of the Bankruptcy Act, are involved.

Summary of Argument.

(1) Questions of local state law:

(a) The Attorneys have agreed that the *amount* of their compensation is to be fixed by the federal reorganization court. Their contract was not abrogated by a wrongful discharge. They were permitted to complete the services for which they had been employed. (Point I.)

(b) Section 475 of the New York Judiciary Law does not grant a *lien* under the circumstances of this case. (Point II.)

(2) Questions of federal law:

(a) The Attorneys are bound by the plan of reorganization and the order confirming it, both of which provide that the federal reorganization court shall fix the fee of the Attorneys. The federal court order and plan are *res judicata* and cannot be attacked collaterally in a state court. (Point III.)

(b) Even if no implied or express agreement gives it such jurisdiction, the federal reorganization court has exclusive jurisdiction to fix the compensation of attorneys appointed by it to assist its Trustees in the collection of assets by suits in state courts. (Point IV.)

(c) No lien on assets of a debtor can be secured during the pendency of a proceeding under Chapter X of the Bankruptcy Act. (Point V.)

(d) No state court, without the consent of the reorganization court, may enforce a lien against assets of a debtor during the pendency of a proceeding under Chapter X. (Point VI.)

(e) The United States District Court and the Trustees did not, directly or indirectly, confer jurisdiction upon the state court to fix the *amount* of the allowance to be made to the Attorneys; nor did they confer jurisdiction upon the state court to enforce any claimed *lien*. (Point VII.)

(f) The case of *Sherman* v. *Buckley* and the *Cup Craft* cases are not in point. (Point VIII.)

(g) No other federal or state court decisions are in conflict with the decision of the state court herein. (Point IX.)

POINT I.

The Attorneys have bound themselves by contract to the fixation of their fees by the federal reorganization court.

The Attorneys herein agreed to the fixation of their compensation by the federal reorganization court.

The plan of reorganization provides* (R. 52):

> "All claims in favor of the Debtor or of the Debtor's estate not settled or adjusted in the reorganization proceedings, or in the plan, or in connection with the consummation of the plan, shall be retained and enforced by the Trustees. * * *
>
> "The Court will retain continuing jurisdiction over such claims and the prosecution thereof * * * The Court will from time to time fix the reasonable compensation to be paid to the Trustees, *and their attorneys or counsel*, for services in the prosecution of such claims, * * *"

The Attorneys concede that the "claims" referred to in these provisions of the plan are the claims for the prosecu-

* These provisions are required by sections 216(13) and 221(4) of the Bankruptcy Act.

tion of which they seek compensation in the state court. They claim the benefits of another portion of the same paragraph of the plan from which the foregoing quotations have been taken—that portion of the paragraph under which the reorganized Debtor "is compelled to keep available $300,000 of its assets to assure payment of expenses incurred in the prosecution of these claims" (R. 52).

There were no other claims. The claims prosecuted in the Virginia action were the same claims—asserted against directors against whom service of process could not be made in New York.

The Attorneys approved the plan as early as November, 1939, and urged the creditors and stockholders represented by them to approve and accept it (R. 30).* The plan was confirmed by order dated June 17, 1940, and was consummated in 1940, with the active support of the Attorneys (R. 30).*

As the Attorneys approved the foregoing provisions of the plan, under which it was specified that their fees would be fixed by the federal court, before they conducted the trial of the New York action or performed the most important part of their services, the condition that their fee be fixed by the federal court was a part of their contract with the Trustees and the federal court. The state Court of Appeals so held (R. 128):

> "* * * would appear that both as a matter of law and as a matter of fact the retainer of these attorneys was subject to the condition that the amount of

* These allegations in paragraphs 11 and 12 of the Trustees' answer were expressly admitted in the reply of the Attorneys (R. 68).

any fees would be fixed by the United States District Court."

In addition, when the Attorneys accepted appointment by the federal court, the provisions of the Bankruptcy Act requiring the federal court to fix their fees became, by implication, a part of their contract. In its opinion the New York Court of Appeals said (R. 126):

> "Also, since these attorneys were appointed by the court in this reorganization proceeding and nothing was said as to fees, the services of the attorneys were undertaken subject to all the provisions of the Bankruptcy Act with respect to the compensation for such services. * * * Under such circumstances, even if no exclusive jurisdiction had been given to the Federal Court, the attorneys would in the normal course return to have their compensation fixed by the court by whom their appointment had been made."

In the state court the Attorneys conceded that if there were no wrongful discharge of the Attorneys by the Trustees, the state court would have no jurisdiction to fix their compensation. But they contended that under the state law they had been wrongfully discharged by the Trustees, and that such discharge abrogated their contract that the federal reorganization court was to fix their compensation, and gave jurisdiction to the state court.

The precise position taken by the Attorneys is shown by the following quotation from pages 7 and 8 of their brief on their motion for a reargument in the state Court of Appeals:

"Judge Finch, in the prevailing opinion, states that respondents fully performed the services for which they were retained. On that assumption he deems the issue presented on this appeal to be whether the New York Court had the power to grant an allowance to respondents for such completed services, and concludes that exclusive jurisdiction resided in the Bankruptcy Court. The facts as found by both courts below, however, are that respondents were discharged prior to the full performance of their services, that the actions which they were retained to prosecute were not completed and that appellants sought to substitute themselves in place of respondents in the pending New York actions.

"The issue on this appeal, therefore, is not whether the State Court has jurisdiction to grant allowances in general to attorneys appointed by the Bankruptcy Court after services have been completed by such attorneys. *On that proposition there is no dispute; where an attorney appointed by a Bankruptcy Court has completed his work, the fixing of his compensation and the granting of allowances are made by the Bankruptcy Court and all the provisions of the Bankruptcy Act referred to by Judge Finch, relating to allowances to attorneys in the Bankruptcy Court, become effective.*"

A. The Attorneys' Contract Was Not Abrogated by a Wrongful Discharge.

The Court of Appeals held that, as a matter of local state law, the Attorneys had not been wrongfully discharged, but had been permitted fully to perform the services for which they had been employed. The Court said (R. 128):

"* * * the attorneys herein were permitted fully to perform the services for which they were appointed, namely to reduce the claims to judgment. * * *"

It therefore appears that the state Court of Appeals held, as a matter of state law: (1) that the Attorneys were bound by contract to have their fee fixed by the federal reorganization court; and (2) that the contract had not been abrogated by a wrongful discharge of the Attorneys.

B. The Attorneys' Contract Is Not Abrogated by Section 475 of the New York Judiciary Law.

The contractual rights of attorneys, as to *amount* of compensation or method of fixing such compensation, are not affected by the provisions of Section 475 of the New York Judiciary Law. The section merely extends the common law charging lien of an attorney, in an appropriate case, by granting such lien as soon as the attorney's services commence instead of when the judgment is entered. *Matter of Heinsheimer*, 214 N. Y. 361.

Section 474 of the same law expressly provides that "the compensation of an attorney or counsellor for his services is governed by agreement, express or implied, which is not restricted by law", except where the services are rendered to the guardian *ad litem* for an infant.

POINT II.

Section 475 of the New York Judiciary Law does not grant a lien under the circumstances of this case.

In an excellent opinion on the nature of attorneys' liens, Judge Cardozo, in *Matter of Heinsheimer*, 214 N. Y. 361, at page 365, said that Section 475 of the New York

Judiciary Law merely enlarges the common law charging lien of an attorney "to the extent that it now attaches to a cause of action even before judgment" (p. 365). He stated, quoting with approval from a previous New York case, that such a lien is a "device invented by the courts for the protection of attorneys against the knavery of their clients" (p. 365) and (quoting from an English case) that "the facts of the case must be looked at to see whether the solicitor * * * has made with his client an arrangement which sufficiently indicates the intention of the parties that the right shall no longer be enforced" (p. 367). He stated (p. 368) that "a charging lien cannot exist unless it is an element, express or implied, of the agreement, that the lawyer is to be paid out of the fruits of the judgment".

Judge Cardozo held that an agreement under which an attorney is to receive periodic payments from his client is inconsistent with an intent that the attorney should have a lien under Section 475.

So, too, in this case, the facts are inconsistent with any intent that the Attorneys should have a lien.

The statute (Bankruptcy Act, Section 216 (3)) provides that the claim of the Attorneys, as an expense of administration, must be paid in full.

In addition, as stated by the Attorneys (R. 19, 20), the reorganized debtor, under the plan confirmed by the reorganization court with the active support of the Attorneys, "is compelled to keep available $300,000 of its assets to assure payment" of their claim.

The reorganization court, with the consent of the Attorneys, thus provided a special fund for the protection of the Attorneys, and it is not "an element, express or implied, of the agreement, that" they are "to be paid out of the fruits of the judgment".

POINT III.

The Attorneys are bound by the plan of reorganization and the order confirming it, both of which provide that the federal reorganization court shall fix the fee of the Attorneys. The federal court order and plan are *res judicata* and cannot be attacked collaterally in a state court.

The plan of reorganization provides that the federal reorganization court retains jurisdiction to "fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of" the claims prosecuted by these Attorneys (R. 52).

The plan also provides only for the payment of claims of creditors which have been proved in the proceedings and for the payment of such reorganization debts and expenses as are allowed by the federal reorganization court (R. 37, 55).

The order confirming the plan of reorganization provides that costs and expenses of administration shall be paid only if approved by the reorganization judge after a hearing upon proper notice under the Bankruptcy Act (R. 66).

The Attorneys are bound by the foregoing provisions of the plan and of the order confirming the plan. They were parties to the reorganization proceeding. They participated in the formulation of the plan and order of confirmation. They urged the court and the security holders' committees represented by them to approve and accept the plan and the order confirming it. Their time to appeal has long since expired. No appeal was taken.

The Attorneys have not filed or proved their claim in the reorganization proceeding. No claim by them has been approved by the reorganization judge.

Even if the federal reorganization court had acted beyond its power in confirming a plan containing these provisions—as was not the case—the Attorneys are bound by the plan and the order which confirmed it, which are *res judicata* as to them. They cannot attack the plan or order collaterally in a state court. *Stoll* v. *Gottlieb*, 305 U. S. 165.

POINT IV.

The United States District Court has sole power to fix the compensation to be paid to the Attorneys, as its agents and officers in the administration of the reorganization estate.

The Attorneys were appointed by the United States District Court to assist in the administration of the estate—to assist in the liquidation of assets. They are officers and agents of said Court.

Every court has exclusive control over the compensation to be paid out of assets administered by it to attorneys or officers appointed by it.

The case of *Fanning* v. *Poe*, 76 F. (2d) 707, is on all fours with the case now before this court, except that the positions of the state and bankruptcy courts were reversed.

In that case, a state court appointed receivers of the assets of a partnership. The partnership had a claim against a bankrupt. The state court authorized its receivers to employ an attorney to prosecute in the bankruptcy proceedings the claim of the state court receiver.

Subsequently, a controversy arose between the state court receivers and their attorney, appointed by the state court, as to the amount of the attorney's fee. The attorney, without submitting the matter to the state court, made an application to the bankruptcy court, asserting a lien on the claim. The referee in bankruptcy sustained the attorneys and recognized a lien.

Upon review, the lower federal court and the Circuit Court of Appeals reversed the referee. They held that only the court appointing the attorney could fix the amount of his fees. The United States Circuit Court of Appeals, in its opinion, 76 F. (2d) 707, at page 709, said:

> "Appellant is an attorney and counselor at law, appointed by and subject to the authority of a state court. * * * He may not take that appointment as the source of his authority to appear in the bankruptcy court, and, without permission of the court appointing him, look elsewhere for the fixing of his fees for so appearing. * * * An appointee of that court, he could not have retained any part of the moneys that court had authorized him to collect for it, except with its approval. *Lynde* v. *Lynde*, 64 N. J. Eq. 736, 52

A. 694, 58 L. R. A. 471, 97 Am. St. Rep. 692; *In re Gilbert*, 276 U. S. 294, 297, 48 S. Ct. 309, 72 L. Ed. 580; *In re Debbins* (D. C.), 53 F. (2d) 1018."

Congress in the exercise of its power over bankruptcies has, by statute, expressly recognized the foregoing principle and has vested bankruptcy and reorganization courts with exclusive power over the compensation of attorneys appointed by them.

Section 241 of Chapter X of the Bankruptcy Act gives control over the compensation of attorneys for trustees to the judge of the reorganization court.

Section 62 of the Bankruptcy Act, which is applicable to proceedings under Chapter X, provides (in subsection a) that the "actual and necessary costs and expenses incurred by officers in the administration of estates * * * be reported in detail, under oath, and examined and approved or disapproved by the court" (referring to the bankruptcy court). It also requires (in subsection d) that a trustee, or an attorney for the trustee, "or any other attorney, seeking compensation for services rendered by him in a proceeding, shall file with the court his petition setting forth the value and extent of services rendered, the amount requested and what allowances, if any, have theretofore been made to him."

Supplementing the foregoing sections, Section 221(4) of Chapter X of the Bankruptcy Act provides that the judge cannot confirm a plan of reorganization unless satisfied that all "costs and expenses in, or in connection with, the proceeding, or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable, or if to be fixed after con-

firmation of the plan, will be subject to the approval of the judge."

In this case, the plan has been confirmed. The amount to be paid for the services of the Attorneys is therefore "subject to the approval of the judge" (of the reorganization court).

Under these statutory provisions, attorneys employed to assert claims in behalf of a bankruptcy or reorganization estate in other courts must apply to the bankruptcy court for the fixation and allowance of their fees.

This Court, in *Page* v. *Rogers*, 211 U. S. 575, said that "the proper place to raise" the question as to the amount to be paid to the attorney for a bankruptcy trustee for services in a separate equity action was "in the bankruptcy court" and not in the equity court (p. 581).

In *Watkins* v. *Sedberry*, 261 U. S. 571, the trustee in bankruptcy had employed an attorney to prosecute a suit in a state chancery court to recover certain assets. The Court said (p. 575) that the attorney's fee for services in the state court action was "an expense of administration" of the bankruptcy proceeding, and was "subject to the examination and approval" of the bankruptcy court.

In *Davidson* v. *Friedman*, 140 Fed. 853, the attorney rendered services in the realization of assets for the trustee. The court, at page 853, said:

> "The matter involved in the present appeal is an expense incurred by the trustee in the course of his administration."

In *In re Stemper*, 222 Fed. 690, an attorney was employed to bring an action in behalf of a bankruptcy trustee in a state court to recover on an insurance policy. The court, at page 692, said that the attorney could not acquire "any rights in or to such assets which were not subject to the control of the court [the bankruptcy court]." It also said:

> "It is elemental law that an attorney, performing services for a trustee which he claims shall be paid out of the trust estate, must submit his claim, so far as it affects the assets of the trust estate, to the court, and that any payment to him by the trustee must be in accordance with an order of the court."

Section 247 of Chapter X requires that notice of hearing for the consideration of an application by an attorney for a trustee or the debtor for an allowance, be given to the debtor corporation, the creditors, the stockholders, indenture trustees, the Securities and Exchange Commission, and other interested persons. Section 206 gives all such persons a right to be heard on the application.

The need for these provisions is evident. The trustees have no direct financial interest in the debtor's estate. Numerous creditors and stockholders are the real parties in interest. The reorganized debtor has a very important interest. They should all have an opportunity to be heard on applications which will diminish the estate to be distributed to them.

In the reorganization proceedings they are given this opportunity. In a proceeding before the state court, no such opportunity is given.

Also, the Securities and Exchange Commission is an adviser to the reorganization court on all applications for allowances. It has no standing before the New York court.

Other safeguards are provided in the reorganization proceedings which are not applicable to proceedings in the state court.

That the compensation and other provisions of Chapter X apply to all attorneys who perform services in the administration of the estate, regardless of whether they represent the trustees only in conducting the proceeding under Chapter X, clearly appears from Section 157 of Chapter X. This section expressly recognizes that attorneys for trustees may perform services either in the proceeding itself or in other actions. It specifies different qualifications for attorneys performing services in the proceeding itself and for attorneys performing services in other actions or outside the proceedings.

The power of Congress to vest in the reorganization court exclusive jurisdiction over the compensation to be allowed to attorneys appointed by it to assist its trustees in the administration of the reorganization estate cannot be doubted. *In re Chicago, Milwaukee, St. Paul & Pacific Rr.*, 121 F. (2d) 371.

Attorneys appointed by reorganization and bankruptcy courts to conduct litigations in other courts invariably apply to the reorganization and bankruptcy courts for a determination of their fees. This was done in the following cases:

Watkins v. Sedberry, 261 U. S. 571;
In re Evans, 117 Fed. 574;
In re McKenna, 137 Fed. 611;
In re J. M. Fiske, 209 Fed. 982;
In re Stemper, 222 Fed. 690;
In re Cheney, 300 Fed. 465;
In re Levinson, 19 F. (2d) 253;

Watters v. *Hamilton Gas Co.*, 29 F. Supp. 436, 477 (971, 723).

Diligent research has failed to reveal even one case, other than the case now before this court, in which a state court has attempted to fix the amount to be paid for the services of attorneys appointed by a United States District Court in a reorganization or bankruptcy proceeding.

A. The generous allowance by the state court in this case demonstrates the need for supervision by the reorganization court over the fees to be paid to attorneys appointed by it to prosecute claims in other courts.

The undesirability of permitting another court—not directly charged with the obligation of conserving the assets of the estate from which payment must be made—to fix the fees of attorneys to be paid by the estate, is well illustrated by the case now before this court.

The court below knew that only $34,522 had been collected (R. 88) on account of the judgment in the New York action, and that the prospects were that not more than another $150,000 would be collectible. It had knowledge that a proceeding for the settlement of the judgment for $150,000 was pending before the United States District Court and that the papers in such proceeding contained "information regarding the financial responsibility of the defendants against whom the judgments were rendered" (Letter, R. 93, 94; put in evidence, R. 87, 88).

The Attorneys had copies of the foregoing papers in the reorganization proceeding. They did not put them in evidence in the state court proceeding. The state court did not request the production of these papers.

It is no answer to say that the Trustees could have submitted to the jurisdiction of the state court, and could have introduced the papers in evidence. The fact is that the federal statute regulating allowances to attorneys appointed by the reorganization court requires the United States District Judge to protect the interests of the estate; the procedure in the reorganization proceeding would have resulted in a revelation of the facts; and all creditors, stockholders and other interested parties would have been given an opportunity to present facts and be heard on the allowances. In addition, the reorganization court would have postponed making the allowance until all the facts were known, including knowledge of the compensable services rendered by others in the New York action in which the Attorneys performed their services.

The lower state court allowed $102,250 (including interest) to the Attorneys for their services in the Principal Action. After deducting approximately $14,500 for other expenses and disbursements in the action (this amount is none too great—an obligation of $2750 was incurred by the Attorneys for the services of one expert who testified on the value of securities) from the total probable collection of $190,000, the fee awarded to the Attorneys represents more than 58% of the net recovery.

This allowance is completely out of line with allowances sustained in other cases involving services in state court actions by attorneys appointed by bankruptcy and reorganization courts.

Watkins v. *Sedberry*, 261 U. S. 571; *In re J. M. Fiske & Co.*, 209 F. 982; *In re Cheney*, 300 F. 465; *In re Levinson*, 19 F. (2d) 253; *In re Barcelonx*, 9 F. Supp. 146, affd. 74 F. (2d) 288; *In re Paramount-Publix Corp.*, 10 F. Supp. 504.

POINT V.

No lien on assets of a debtor can be secured during the pendency of a proceeding under Chapter X of the Bankruptcy Act.

Liens may not be secured against property subject to the exclusive jurisdiction of a bankruptcy or reorganization court because the court itself has an overriding control over all of the debtor's property which cannot be interfered with by any lien or other assertion of interest in such property. During the pendency of the bankruptcy or reorganization proceeding, the disposition of the property is controlled completely by the court.

In place of liens and other priorities under which claims against the property of the debtor may be secured before the filing of the petition—*i. e.* before the court takes exclusive jurisdiction—a new system of rights is substituted. As stated by this Court in *Prudence Realization Corp.* v. *Geist*, 316 U. S. 89, at page 95, "The bankruptcy act prescribes its own criteria for distribution to creditors".

Section 64 of the Bankruptcy Act specifies the order of priority of the various claims against the property of an estate in an ordinary bankruptcy proceeding. In reorganization proceedings under Chapter X no priority is fixed for claims arising during the administration of the estate because no reorganization may be approved unless provision is made for the payment in full of all costs and expenses of administration (Section 216(3)).

The proper procedure for the enforcement of a claim which would normally be protected by a lien, but which arises during the course of administration by a reorganization court, is indicated in *In re Fonda Johnstown & Gloversville Railroad Co.*, 126 F. (2d) 604. The court held that state franchise taxes accruing during the pendency of the reorganization should be allowed in the reorganization proceeding and paid by the trustee as part of the expenses of administration. See also, *United States v. Wood*, 290 F. 109, aff'd 263 U. S. 680.

That a lien cannot be secured against assets of a bankrupt or debtor during the pendency of a bankruptcy proceeding or a proceeding under Chapter X, is fundamental.

In *Lazarus, Michel & Lazarus v. Prentice*, 234 U. S. 263, a lien against assets in the possession of a bankruptcy court was asserted by virtue of transactions which occurred after the filing of the petition in bankruptcy. This Court held that no lien could arise after the initiation of the bankruptcy proceeding. At page 266 of its opinion, the Court said:

> "The filing of the petition and adjudication in the bankruptcy court in New York brought the property of the bankrupts, wherever situated, into *custodia legis*, and it was thus held from the date of the filing of the petition, so that subsequent liens could not be given or obtained thereon, nor proceedings had in other courts to reach the property, the court of original jurisdiction having acquired the full right to administer the estate under the bankruptcy law. *Muller v. Nugent*, 184 U. S. 1, 46 L. ed. 405, 22 Sup. Ct. Rep. 269; *Acme Harvester Co. v. Beekman Lumber Co.*, 222 U. S. 300, 56 L. ed. 208, 32 Sup. Ct. Rep. 96."

In *Straton* v. *New*, 283 U. S. 318, this Court, at page 321 of its opinion, said:

> "* * * The filing of the petition is an assertion of jurisdiction with a view to the determination of the status of the bankrupt and a settlement and distribution of his estate. This jurisdiction is exclusive within the field defined by the law, and is so far *in rem* that the estate is regarded as in *custodia legis* from the filing of the petition. *Acme Harvest Co.* v. *Beekman Lumber Co.*, 222 U. S. 300, 56 L. ed. 208, 32 S. Ct. 96. It follows that liens cannot thereafter be obtained nor proceedings be had in other courts to reach the property, the district court having acquired the exclusive right to administer all property in the bankrupt's possession."

Only in one situation may a lien be perfected after the filing of the petition. Section 67b of the Bankruptcy Act provides that "statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof * * * may be valid against the trustee even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition * * * where * * * such liens * * * arise but are not perfected before bankruptcy, * * * if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property they shall instead be perfected by filing notice thereof with the court".

Any lien granted by Section 475 of the New York Judiciary Law is a statutory lien and falls within the provisions of Section 67b of the Bankruptcy Act. When

a lien arises under this statute before the filing of the petition in bankruptcy or reorganization, the formal procedure of perfecting the lien may occur after the filing of the petition if the lien can be perfected without seizure of the assets.

The cases of *Sherman* v. *Buckley*, 119 F. (2d) 280; *In re Cup Craft Paper Corporation*, 40 Fed. Supp. 927, and *Cup Craft Paper Corp.* v. *Federal Paper Board Co.*, 262 App. Div. 91, aff'd 289 N. Y. 671; *In re Cup Craft Paper Corp.*, 40 F. Supp. 927, aff'd sub. nom. *New York Credit Mens Assn.* v. *Schlesinger*, 126 F. (2d) 472; are cited by the Attorneys. *All* of these cases come squarely within the provisions of Section 67b. In all of these cases the lien arose prior to the filing of the petition in bankruptcy and the state court merely perfected the lien after the initiation of the bankruptcy proceedings.

In the case now before this court no lien arose prior to the filing of the petition which could be perfected after the filing of such petition.

Even where Section 67b of the Bankruptcy Act is applicable, the statute expressly provides that a lien cannot be perfected by a seizure of property of the debtor although the state law requires such seizure. In such cases the lien is perfected by a notice filed with the bankruptcy court. There can be no interference with the property by or through any other court or agency.

POINT VI.

No state court, without the consent of the reorganization court, may enforce a lien against assets of the debtor during the pendency of a proceeding under Chapter X.

Effective reorganization calls for a single agency, with complete and paramount jurisdiction over the debtor and its property, to administer the assets while the proceeding is pending and to determine all claims against the debtor or its assets.

Reorganization requires a more complete control and more inclusive jurisdiction than the court in an ordinary bankruptcy possesses. A corporation which seeks the aid of a court to effect a reorganization generally has pledged or mortgaged most of its property. It would be futile to essay a reorganization of such a corporation without including the assets which are subject to mortgages or liens. In most instances, a successful reorganization can be accomplished only if all the creditors, secured and unsecured, and all the property, whether subject to lien or not, are included.

Chapter X recognizes this need. Under express statutory provisions, the court in a reorganization proceeding under Chapter X has wider jurisdiction than in an ordinary bankruptcy proceeding.

Section 111 of the Bankruptcy Act gives to the reorganization court "exclusive jurisdiction of the debtor and its property, wherever located".

All pending bankruptcy, mortgage foreclosure, and equity receivership proceedings, and other proceedings to enforce liens against property of the debtor, are automatically stayed by the mere filing of the petition initiating the Chapter X proceedings (Section 148). Receivers and trustees appointed by state or federal courts, trustees under trust deeds, and mortgagees under mortgages, having possession of property of the debtor, must immediately recognize the superior jurisdiction of the court in the Chapter X proceeding by surrendering such property to the trustee in the Chapter X proceeding (Section 257). The court may authorize its receiver or trustee to borrow money and may authorize him to issue certificates secured by a lien on the debtor's property which may be given priority over all existing mortgages and other liens (Section 116(2)). The plan approved by the court may alter or modify the rights of secured creditors, satisfy or modify liens, direct the transfer or sale of any part of the property, cancel or modify indentures and similar instruments, and change interest rates and other terms of outstanding securities (Section 216). The court may direct mortgagees, indenture trustees, and others, to execute and deliver such instruments as may be necessary to satisfy liens or transfer property in consummation of a plan (Section 227).

All of the foregoing powers are completely inconsistent with an assertion by a state court of power to appropriate assets of the debtor to the satisfaction of liens. As the bankruptcy statute is paramount, the state court must yield its ordinary jurisdiction to the superior jurisdiction of the reorganization court. *Kalb* v. *Feuerstein*, 308 U. S. 433.

Even in an ordinary bankruptcy proceeding, no other court may, during the pendency of the proceeding, take jurisdiction of an action to enforce a lien against the assets of the bankrupt, without the consent of the bankruptcy court.

> "Though a lien be not discharged by bankruptcy, its owner may not, without the bankruptcy court's permission, institute proceedings in a state court to enforce it, since his so doing might interfere with the orderly administration of the estate."
>
> *Straton* v. *New*, 283 U. S. 318, 321.

> "Thus, while valid liens existing at the time of the commencement of a bankruptcy proceeding are preserved, it is solely within the power of a court of bankruptcy to ascertain their validity and amount and to decree the method of their liquidation."
>
> *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 738.

Even if the state itself desires to assert a tax lien against assets of the debtor corporation, it must do so in the reorganization proceedings, otherwise it loses its rights. *New York* v. *Irving Trust Co.*, 288 U. S. 329, 333; *Van Huffel* v. *Harkelrode*, 284 U. S. 225-228.

The cases of *Matter of Atterbury*, 222 N. Y. 355, and *Matter of King*, 168 N. Y. 53, cited in the Attorneys' brief, are not in conflict with the foregoing principles.

Neither case involved the paramount jurisdiction of a United States District Court in a proceeding under Chapter X of the Bankruptcy Act. Neither case involved an attorney appointed by a court to assist such court in the administration of an estate.

In the case of *Matter of Atterbury* the administrator was appointed by the court to bring an action under Section 130 of the New York Decedent Estate Law for the benefit of the next of kin for damages for the wrongful death of decedent. The attorney was selected by the administrator.

In *Matter of King*, the trustee was trustee of a testamentary trust. The trustee selected the attorney.

In each case the courts involved were courts of concurrent jurisdiction, where, accordingly, either court securing jurisdiction retains that jurisdiction to the exclusion of other courts. The cases are not applicable to a situation where a valid statute gives to one of the courts exclusive jurisdiction of the assets regardless of which court first took jurisdiction.*

No case is cited in which the reorganization court, with its statutory "exclusive" jurisdiction, has been held to lose its jurisdiction over particular assets merely because it has submitted specified questions—not involving the same issues—and arising between different parties—to a state court for adjudication.

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* The lower state court herein was led into error as to the effect to be given to these cases by its assumption that the state court and the reorganization court have concurrent jurisdiction over assets of the debtor. It stated, as the rule applicable to the reorganization court in this case, that its "exclusive jurisdiction to deal with the property of the bankrupt estate is but an application of the broader rule that when a court of competent jurisdiction takes possession of property for the purpose of administering it no other court can then interfere with or disturb that possession", and that "when a state court at the time bankruptcy occurs already is proceeding to ascertain and enforce liens of a kind not invalidated by the bankruptcy * * * the bankruptcy does not oust the state court of its jurisdiction or vest the bankruptcy court with power to enjoin its proceedings" (R. 105). Obviously, this is not a correct statement of the basis or extent of the exclusive jurisdiction of the court in a proceeding under Section 77B or Chapter X.

A. Section 475 of the New York Judiciary Law does not give a state court jurisdiction to enforce an attorney's charging lien against causes of action which are assets of a debtor, during the pendency of a proceeding under Chapter X.

Section 475 of the Judiciary Law merely extends the common law charging lien of an attorney by granting such a lien at the inception of the action in which the services are rendered instead of when judgment is entered (*Matter of Heinsheimer*, 214 N. Y. 361). As the Attorneys did not assert their claim until after entry of the judgment in the New York action brought in behalf of the reorganization estate, their rights are neither greater nor less than they would be under the common law. There is no particular magic therefore in the fact that they are relying on a statute.

The charging lien of an attorney—when it exists*—is no more sacred than a mechanic's lien, or a landlord's lien, or a tax lien. State courts have jurisdiction over all of these—normally—when such jurisdiction has not been superseded by the paramount jurisdiction of a federal court in proceedings under Chapter X. No state court may, however, enforce *any* lien against the assets of a debtor after the approval of a petition under Chapter X, without the consent of the reorganization court. Even sovereign states must look to the reorganization court for the satisfaction of their tax liens, and if they fail to file their claims *in the proceedings in the reorganization court* before the expiration of the bar date fixed by such court, the claims cannot be asserted against assets of the debtor. *New York* v. *Irving Trust Co.*, 288 U. S. 329; *Van Huffel* v. *Harkrode*, 284 U. S. 225.

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* That the Attorneys have no lien appears from the discussion on pages 16-18 of this brief.

POINT VII.

The United States District Court and Trustees did not, directly or indirectly, confer jurisdiction upon the state court to fix the *amount* of the allowance to be made to the Attorneys; nor did they confer jurisdiction upon the state court to enforce any claimed *lien*.

The New York Court of Appeals has held (R. 128): (1) that there was "no waiver by the Federal court under the circumstances in the case at bar" of its "exclusive jurisdiction" "to determine these fees"; (2) that "from first to last the trustees herein have insisted upon their claim that in the case at bar jurisdiction to make allowances to these attorneys did not reside in the State court but resided in the Federal court"; and (3) that "it is unnecessary to consider whether it was within the power of the court to surrender this jurisdiction, since it would appear that both as a matter of law and as a matter of fact the retainer of these attorneys was subject to the condition that the amount of any fees would be fixed by the United States District Court".

There was therefore no *direct* waiver of jurisdiction by the federal reorganization court.

Was there an *indirect* waiver by reason of the litigation conducted in the state court by the Attorneys, in behalf of the reorganization estate, against the old Reynolds directors?

A. Effect of the submission of the controversy with the Reynolds directors to the jurisdiction of the state court.

When the reorganization court permitted the Debtor and the Trustees to institute and prosecute the action against the old Reynolds directors in the state court, it necessarily submitted to that court jurisdiction over all the issues in that action. The Debtor and Trustees were bound by the adjudication in that case: If costs had been assessed against them in that case, they would have been bound to pay such costs. If, as in *Sherman* v. *Buckley*, the Trustees had made an application in that action for an order of substitution, or any other order, and the court had imposed a condition in the order, granting the application,* the Trustees would have been bound by such condition if they had acted under the order without taking an appeal.

But surrender by the reorganization court of jurisdiction over particular issues to the state court—in this case, the issues in the controversy with the old Reynolds directors—did not constitute a general surrender of its exclusive jurisdiction over the administration of the causes of action as assets of the reorganization estate.** When

* In *Sherman* v. *Buckley*, 119 F. (2d) 280, the bankruptcy trustee applied for an order for the substitution of attorneys in the state court action. The order granting substitution expressly gave the superseded attorneys a lien for 30% of the ultimate recovery. The trustee and his substituted attorneys took no appeal, but acted under the order for more than five years.

In the case at bar, no application was made for an order of substitution, and no order of any kind, giving the attorneys a lien or fixing the amount of their compensation, was made in the state court action authorized by the reorganization court.

** Surrender of jurisdiction over the Reynolds issues to a New York court was necessary. The process of the reorganization court (the United States District Court for the District of New Jersey) was not effective in New York, where the necessary defendants resided and had their places of business.

the issues submitted to the New York court had been determined, and final judgment had been entered, the jurisdiction of the New York court came to an end.

Even before final judgment in the New York action, only the reorganization court could administer the causes of action as assets of the debtor. The New York courts could not pass upon claims of third parties against these assets. They could not authorize a settlement, or sale, or other disposition of the causes of action.

Causes of action are, obviously, assets of the reorganization estate which, like all other assets, are subject to the exclusive jurisdiction of the reorganization court. *Gochenour* v. *Cleveland Terminals Bldg. Co.*, 118 F. (2d) 89.

Chapter X itself, in Section 216(13), expressly recognizes causes of action as assets subject to the jurisdiction of the reorganization court. It provides that "such claims not settled or adjusted in the plan" shall be retained and enforced by the reorganization trustee.

The proceeding, which the Attorneys brought in the New York court, *after* the termination of the Reynolds action, was a separate and independent proceeding—conducted as an independent action—with different parties and issues. It was not, and could not be, a motion in the Reynolds action which had been authorized by the reorganization court.

As stated by the court in *Peri* v. *New York Central Rr.*, 152 N. Y. 521, at page 526, the proceeding by an attorney to enforce his lien,

"* * * is a special proceeding and cannot be

regarded in any proper sense as a motion in the action. * * *

"We have here a proceeding by third parties against the defendant upon other issues than those framed in the action and relating to a lien arising out of a state of facts wholly distinct from those passed upon at the trial. * * *

"'It is conducted as if it were an independent action.'"

Jurisdiction of the court over the parties in the action in which the attorney's services were rendered does not carry over into the special proceeding to enforce the attorney's lien. New personal service must be made as in the case of a summons (Rule 21 of New York Rules of Civil Practice).*

In the case at bar, the Attorneys seek in this separate proceeding to recover for the value of services rendered in three different New York actions, each action having different parties and involving different issues.

Even where a bankruptcy trustee appeared in a state court action and successfully moved that such action be transferred to a federal equity court, he was not precluded from thereafter successfully asserting that the equity court did not have jurisdiction because of the ex-

* It is true that Justice Walter presided at the trial of the issues in the principal Reynolds action, and also passed upon the merits of the application of the Attorneys for the enforcement of their claimed lien. But this was purely accidental. Such applications are heard in Special Term, Part I, of the New York Supreme Court. Justice Walter just happened to be sitting in this Part on January 12, 1942, the date on which the Attorneys made their application returnable. In the two entire calendar years of 1941 and 1942, Justice Walter sat in that Part a total of only five weeks: the weeks commencing April 28, 1941, August 18, 1941, *January 12, 1942*, January 19, 1942, and August 24, 1942.

clusive jurisdiction of the bankruptcy court. *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 739.

B. Power of a Reorganization Court to waive its jurisdiction.

The power of a bankruptcy or reorganization court to delegate its powers or waive its jurisdiction is extremely limited.

Its jurisdiction over such matters of administration as the fixing of the fees of its agents and attorneys may not be delegated or waived. See *U. S. Fidelity & Guar. anty Co.* v. *Bray*, 225 U. S. 205, 217, 218; *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 739; *Gross* v. *Irving Trust Co.*, 289 U. S. 342, 344; *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, 483.

Section 241 of the Bankruptcy Act expressly puts upon the reorganization judge the duty of fixing the fees of attorneys appointed by him to assist the trustees in the administration of the estate. It is the discretion of the district judge—not the discretion of any other person or tribunal—which the statute demands. The district judge cannot avoid this obligation by delegation to another court. He cannot even delegate it, under a plan, to the trustees or committees in the proceedings (*Wright* v. *City National Bank & Trust Co.*, 104 F. (2d) 285).

Even if the reorganization judge had power to delegate this important administrative function, he could, at most, delegate only his own power. He could not evade the clear mandate of statute and court rule by delegating the matter to another court free from the restrictions imposed upon him by Sections 62, 206, 247 and 249 of the

Bankruptcy Act and General Order in Bankruptcy 44. The requirements of these statutes and rules were not met in the proceeding in the state court.

In unusual situations—such as where state law must be applied and such law is unsettled—the reorganization or bankruptcy court may permit specific issues to be litigated in a state court. A lower federal court may even be reversed on appeal by this Court or the Circuit Court of Appeals for failure to exercise its power to permit litigation in a state court where justice or equity demands such litigation (as in *Foust* v. *Manson S. S. Lines*, 299 U. S. 77). But in each case, where a higher federal court reversed for failure to permit a state court action, the controversy involved a claim against a debtor or bankrupt which arose prior to the reorganization or bankruptcy proceeding; it did not involve a debt or expense of administration. And in each case it was recognized that the *reorganization or bankruptcy court* must expressly give its permission.*

This Court has recently held that it is error for a federal court, having exclusive jurisdiction over a matter, to refuse to take jurisdiction because state law is involved and such law can not be determined because of the absence of state court decisions (*Meredith* v. *Winter Haven*, 88 Supreme Court Law ed. Advance Opinions page 1). The proper procedure is for the federal court to take jurisdiction, instruct the parties by appropriate action to get a state court ruling on the disputed questions of state law, and then administer the estate in con-

* If the federal court improperly refuses permission, the remedy is by appeal and reversal. Without affirmative permission the state court does not acquire jurisdiction. See *Palmer* v. *Larchmont Manor Co.*, 284 N. Y. 288.

formity with the state law as thus established (*Mangus* v. *Miller*, 317 U. S. 178).

C. Section 475 of the New York Judiciary Law does not impose a condition upon the right of a reorganization estate or other litigant to use the state courts.

Section 475 of the New York Judiciary Law does *not* impose a condition upon the right of a litigant to use the state courts.

The statute does not exact a lien for the attorney as the price to be paid for the right to litigate issues in the state courts. It merely gives an attorney, when "it is an element, express or implied" of his agreement that he "is to be paid out of the fruits of the judgment", the right to a lien to protect his claim for services. *Matter of Heinsheimer*, 214 N. Y. 361, 368. When it exists, it is a statutory lien similar to a mechanic's lien, a landlord's lien, or a tax lien.

That Section 475 does not purport to attach a condition to the right to use the state courts clearly appears from the fact that it grants a lien whether the services are rendered in federal courts or state courts. It even grants a lien for services rendered before a "federal department". Obviously the state statute cannot attach a condition to the right to use the federal courts or to appear before federal departments.

POINT VIII.

Discussion of the *Cup Craft* and *Sherman* v. *Buckley* cases.

The Attorneys seek to justify their position by a reliance upon the case of *Sherman* v. *Buckley*, 119 F. (2d) 280; and the *Cup Craft* cases (*Cup Craft Paper Corporation* v. *Federal Paper Board Co.*, 262 App. Div. 91, affd. in 289 N. Y. 671; and *In re Cup Craft Paper Corporation*, 40 F. Supp. 927, affd. sub nom. *New York Credit Men's Assn.* v. *Schlesinger*, 126 F. (2d) 472).

The dissenting judges of the New York Court of Appeals based their dissent entirely upon the case of *Sherman* v. *Buckley* (R. 129).

The facts in Sherman v. Buckley.

The following facts appear in the record on appeal to the United States Circuit Court of Appeals in the *Sherman* v. *Buckley* case:

In 1927, one Gould retained Buckley & Buckley as his attorneys to bring an action in a state court under a 50% contingent retainer. Action was started in New York Supreme Court in May, 1927. It was tried in November, 1932. Gould was non-suited. (Record, fols. 28 and 29).

An appeal was taken in Gould's behalf by Buckley & Buckley. Over a year later, while the appeal was still pending, Gould was adjudicated a bankrupt, in January, 1934 (Record, fol. 38).

The trustee in bankruptcy did nothing. The status quo

continued for eleven months—Gould remained as party plaintiff, and Buckley & Buckley remained as attorneys for plaintiff.

On December 10, 1934, the attorneys for the trustee in bankruptcy wrote Buckley & Buckley as follows (Record, fol. 50):

> "Mr. Lyttleton B. P. Gould, the plaintiff in the above-entitled action, informed us that he wishes to substitute us for yourselves as attorneys for the plaintiff in the action now pending in the Supreme Court, New York County. We would suggest that this be done by stipulation which will preserve your lien in the case and leave to future determination by either the court or an arbitrator the amount of such lien."

In January, 1935, the bankruptcy trustee made a motion for a substitution of attorneys. Answering said motion, Buckley & Buckley requested that their lien be fixed in the order of substitution. On February 25, 1935, Justice McGoldrick made an order permitting the substitution of attorneys on condition that Buckley & Buckley have a lien for 30% of any money recovered in the action (Record, fols. 58 to 63).

The bankruptcy trustee did not object to the order. He took no appeal. He acted under the order for a period of five and one-half years. The substituted attorneys and the trustee in bankruptcy acted under the foregoing order, prosecuted an appeal, and secured a reversal of the previous adverse judgment of dismissal; and in October, 1940, secured a settlement which resulted in the entry of a judgment for $40,000 (Record, fols. 150, 151).

Immediately thereafter, also in October, 1940—more than five and one-half years after he had expressly consented to the lien, to the jurisdiction of the state court,

and to the order of the state court fixing the lien—the trustee repudiated his previous consent to the fixing of the lien by the state court and sought an injunction from the Federal court to prevent Buckley & Buckley from asserting rights under the order which had been made by the state court five and one-half years previously. The injunction was granted in the lower court, but was reversed by the Circuit Court of Appeals.

The facts in the Cup Craft cases.

The following facts are taken from the Record on Appeal of the *Cup Craft* case in the New York Court of Appeals:

Schlesinger and Krinsky, attorneys, were retained in 1939 by Cup Craft Paper Corporation to prosecute an action. A written contract of retainer provided that the attorneys were to receive $200 plus one-third of any recovery (Record, fols. 449-452). Suit was commenced in the New York Supreme Court.

In February, 1940, Cup Craft Paper Corporation filed a petition under the Bankruptcy Act. It was adjudicated a bankrupt in May, 1940.

The bankruptcy trustee moved in the state court to be substituted as party plaintiff (Record, fol. 341). The attorneys cross-moved (Record, fols. 356-357) for an order relieving them of further duties in the case and recognizing their lien for services to the bankrupt before his bankruptcy.

The court at Special Term granted the trustee's motion for substitution and the attorneys' motion to be relieved from further duties, but refused to make the order of substitution conditional upon a recognition of the lien of the attorneys for the reasonable value of their services to the bankrupt before his bankruptcy.

The Appellate Division reversed the decision of the Special Term court with the following brief opinion (262 App. Div. 91, 92):

> "*Per Curiam*: The attorneys could not be required, against their will, to represent the Trustee in Bankruptcy in lieu of the plaintiff by whom they were retained (*Matter of Dunn*, 205 N. Y. 398). Upon such a substitution, therefore, the attorneys were entitled to reasonable compensation for services theretofore rendered. The amount of their lien should be referred to an Official Referee to hear and report thereon to the court."

The Court of Appeals affirmed without opinion.

Comparison of this case with Sherman v. Buckley and the Cup Craft cases

The differences which distinguish this reorganization case from the case of *Sherman* v. *Buckley* and the *Cup Craft* cases are:

1. (a) In the *Buckley* and *Cup Craft* cases, the attorneys were not appointed by the bankruptcy court. The services were rendered to bankrupts *before* bankruptcy. (While Buckley continued on the record as attorney for Gould after the bankruptcy of Gould, there is nothing in the record to show that any services were performed by Buckley after the bankruptcy and before the substitution of attorneys—no claim was made for services after the initiation of the bankruptcy proceedings.) The claims were provable as debts of the bankrupts and were not covered by the statutory provisions regulating allowances for services in the administration of a bankruptcy or reorganization estate.

(b) In this case, all the services were rendered in the administration of a reorganization estate; the Attorneys were appointed by the reorganization court as its agents and officers and performed all their services as appointees and agents of said court. The claims were administration debts and expenses covered by the allowance provisions of the Bankruptcy Act, the orders of the reorganization court, and the plan confirmed in the reorganization proceeding.

2. (a) In the *Buckley* and *Cup Craft* cases, the services of the attorneys were rendered and the liens arose *before* the initiation of the bankruptcy proceedings.

(b) In this case, all the services were rendered *after* the initiation of the reorganization proceeding. The alleged lien, if any, arose during the pendency of the federal reorganization proceeding. No lien can arise against assets of a bankruptcy or reorganization estate *after* the initiation of the proceedings.

3. (a) In the *Buckley* and *Cup Craft* cases, liens under Section 475 of the Judiciary Law arose before the filing of bankruptcy petitions and were perfected after the bankruptcy, as expressly permitted by Section 67b of the Bankruptcy Act.

(b) In this case no lien arose prior to the filing of the reorganization petition, and no lien could arise thereafter because the property was then subject to the exclusive jurisdiction of the reorganization court. Section 67b of the Bankruptcy Act only applies to liens arising before the filing of the petition.

4. (a) The *Buckley* and *Cup Craft* cases both involved conditions imposed in orders secured by bankruptcy trus-

tees permitting substitutions of attorneys in state court actions brought by them.

(b) In this case, no order of substitution was requested or granted and no other order in the action brought by the Trustees fixed the compensation of the Attorneys or purported to give them a lien. The order was made in a separate and independent proceeding brought *by the Attorneys* after the action brought by the Trustees had terminated through the entry of judgment; such order was made despite objections made by the Trustees to the jurisdiction of the state court; and appeal was promptly taken.

5. (a) The *Buckley* and *Cup Craft* cases involved the jurisdiction of a bankruptcy court, which has no jurisdiction over property not in its possession, and which has no power to displace valid liens.

(b) This case involves the jurisdiction of a reorganization court under Chapter X of the Bankruptcy Act, which court has exclusive jurisdiction over all the property of the debtor even if it is in the possession of another court. The reorganization court has power to displace valid liens.

6. (a) In the *Buckley* and *Cup Craft* cases, the proceedings were in bankruptcy. In such proceedings no plan of reorganization is confirmed. Liens are not lost unless the court orders a sale free and clear of liens. Such orders had not been entered in either case.

(b) In this case, the proceedings were in reorganization under Chapter X of the Bankruptcy Act. In such proceedings, under Section 226, all claims against the property of the corporation are wiped out except those reserved in the plan and the order confirming the plan. The plan was confirmed June 17, 1940. It provides that only claims

allowed by the reorganization court may be asserted against the property of the debtor.

7. (a) In the *Buckley* and *Cup Craft* cases, the attorneys had contingent contracts, and they were "discharged" before the entry of judgment.

(b) In this case, the Attorneys did *not* have a contingent contract, and they were permitted to completely perform the services for which they had been employed. They entered judgment on the cause of action. They were not "discharged" by the Trustees.

8. (a) In the *Buckley* case, the bankruptcy trustee suggested that the state court grant the lien, made the motion in which the state court fixed the lien, and acted under the order of the state court fixing the lien for 5½ years. By making this motion, acting under it, and not appealing from it, it became *res judicata* as to the trustee.

(b) In this case, the Trustees have at all times contested the jurisdiction and power of the state court to fix the lien. They have not, directly or indirectly, at any time, submitted any phase of their controversy with their attorneys to the jurisdiction of the state court.

9. (a) In the *Buckley* case, the trustee repudiated the agreement which he had made with the attorneys and with the state court.

(b) In this case, the Attorneys repudiate the agreement which they made with the federal court that said court should "from time to time fix the reasonable compensation to be paid" to them "for services in the prosecution of such claims".

POINT IX.

Discussion of the arguments of, and cases cited by, the Attorneys.

The Trustees will discuss under this Point only such matters as have not already been covered in the preceding pages of this brief.

Attorneys' Point I.

The Attorneys place great reliance upon *In re Prudence Co.*, 96 F. (2d) 157.

This case sustains the contentions of the Trustees and not those of the Attorneys. The attorney had been retained by the debtor and suit had been instituted *before* the reorganization proceedings. "When the debtor's petition in reorganization was filed, Mr. Davison had as security for his fees a charging lien on his client's cause of action" (p. 160). "Bankruptcy does not invalidate such liens" (p. 160). The attorney "moved *in the reorganization proceedings* for an order permitting him to receive" payment "in satisfaction of his lien for fees" (p. 159).

Cases which hold that a reorganization trustee must comply with applicable state laws in operating a business, are not applicable. The services of the Attorneys were not performed in the operation of the Debtor's business. They were performed in the liquidation of assets.

The general rule that a receiver or trustee appointed by a court can only be sued with the permission of that

court (*Porter* v. *Sabin*, 149 U. S. 473), applies in the case at bar. The exception to this rule which is embodied in Section 66 of the Federal Judicial Code (28 U. S. C. A. 125) is not applicable, since the services of the Attorneys were not performed "in carrying on the business" of the Debtor. See *Ex parte Baldwin*, 291 U. S. 610, 617, 618.

Attorneys' Point II.

The Attorneys allege that the state court secured jurisdiction because of "the attempt of the Trustees to substitute themselves in place of the Attorneys".

The only basis for this statement is a letter from the Trustees to the Attorneys, dated June 3, 1941 (R. 22, 23), in which the Trustees stated that they did not desire to avail themselves of the services of the Attorneys after the entry of judgment and that they would themselves do whatever might be necessary thereafter to protect the interests of the estate in the causes of the action. The record shows that no application for substitution was ever made to the New York court and no such application was ever considered by it.

The facts now before this court, in this respect, are totally different from those in *Sherman* v. *Buckley*. In that case the Trustee made an application for substitution, consented to the order of substitution and the provision therein under which the lien of the attorneys was fixed, and then operated under the order for a period of five and a half years before repudiating the order.

Attorneys' Point III.

The Trustees have always conceded, and hereby again concede, that the reorganization court did not have jurisdiction (because of the restrictions imposed by Section 23 of the Bankruptcy Act) to pass upon the issues of the plenary action instituted in August 1938* against the old Reynolds directors in behalf of the reorganization estate. The federal court never claimed such jurisdiction. It permitted the Debtor and the Trustees to submit *those* issues to the jurisdiction of the New York court.

But the case at bar does not involve the jurisdiction of the reorganization court over the issues in the controversy with the old Reynolds directors. It involves the jurisdiction of the reorganization court over the fixing of the fees of attorneys appointed by it to assist in the administration of the assets of the estate, and the jurisdiction of the reorganization court over claims against property which is subject to its exclusive jurisdiction. The jurisdiction of the reorganization court over this new controversy is obviously not limited by Section 23. 2 Collier on Bankruptcy (14th ed.) pp. 446-8.

The Attorneys fail to distinguish between the exclusive jurisdiction of the reorganization court over the claim against the Reynolds directors as an asset of the estate — and the jurisdiction of a court to reduce the claim to judgment. They ignore the difference between the summary jurisdiction of the court, and its plenary jurisdiction.

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* This action was commenced, upon authorization of the reorganization court, after the initiation of the reorganization proceeding but before Chapter X became applicable to such proceeding in September 1938.

Obviously, the reorganization court had summary jurisdiction over the claim as an asset, at all times. The Attorneys themselves recognized this jurisdiction. They accepted appointment by the reorganization court and acted under its authority in instituting the action in the New York court. They recognized the exclusive jurisdiction of the reorganization court while the New York action was pending, by acting under its authority in securing a substitution of the Trustees as plaintiff in the New York action in place of the Debtor.

Although the Attorneys quote the language of Judge Maris in *In re Standard Gas & Electric Co.*, 119 F. (2d) 658, they fail to appreciate the distinction which he carefully draws between the exclusive jurisdiction of the reorganization court over the *res* (the claim itself) and claims against that *res*, and the limitation imposed upon a bankruptcy and 77B court by Section 23 of the Bankruptcy Act.

Section 23 limited the power of the reorganization court to try the issues in the action brought by the reorganization estate against the old Reynolds directors. But this does not mean that the causes of action are not assets of the reorganization estate; nor does it mean that the reorganization estate does not have exclusive jurisdiction over these causes of action as part of the *res* which is subject to its exclusive jurisdiction.

The reorganization court may be compelled to use another court to liquidate and establish the claim. But control over the claim—the exclusive power to authorize its settlement, or sale, or other disposition—the exclusive power to determine claims against it as an asset of the

estate—was at all times solely with the reorganization court.

The Chandler Act, in 1938, did not change the exclusive jurisdiction of the reorganization court over allowances to attorneys appointed by it, or over claims against property of the debtor. Such jurisdiction is the same in a proceeding under Section 77B as it is in a proceeding under Chapter X.

If the rights of the parties in this case depend on whether the reorganization court has the jurisdiction of a Section 77B or a Chapter X court—it is difficult to see how they do—then this reorganization court has all the jurisdiction conferred by Chapter X, since the petition and amended petition were "approved as duly and in good faith filed under Chapter 10 of the Bankruptcy Act of 1938" (R. 57), by order dated January 19, 1939. The controversy with these Attorneys arose in 1941, more than two years after the reorganization court commenced to exercise the powers of a Chapter X court.

Attorneys' Point IV.

The Attorneys, in asserting that "the drastic change of nullifying local attorneys' lien laws cannot be found in any of the provisions of Chapter X", imply that an attorney's lien is more sacred than any other lien, such as a tax lien or landlord's lien. Obviously, that is not the case. *No* lien can be secured during the pendency of the reorganization proceeding. No other court may interfere with the assets of a reorganization court in order to enforce a lien against such assets.

An attorney who has accepted appointment by a reorganization court is even less entitled to challenge the jurisdiction of the reorganization court over assets entrusted to him by said court, than a complete outsider whose claim does not stem from a recognition of the jurisdiction of such court.

Attorneys' Point V.

The Attorneys contend in their brief that they are not bound by the plan because they "were never parties to the Plan of Reorganization".

They were attorneys for the most important creditors' committee (representing the bondholders) and for the most important stockholders' committee (representing the preferred stockholders), and received allowances totalling $36,000 for their services in the reorganization proceeding (R. 28). They "approved the aforesaid provisions [of the plan which stated that the reorganization court would fix the amounts of their fees], and have at all times since approved similar provisions. * * *. They have, from time to time, urged the Court, the holders of debentures and shares of preferred stock and other interested parties, to approve and accept plans containing such provisions. They have never, directly or indirectly, expressed disapproval or lack of acquiescence with respect to the aforesaid provisions. The plan which was finally confirmed and actually consummated in 1940 with the entire support of applicants [the Attorneys], contains" these provisions.*

* These allegations are in paragraphs 11 and 12 (R. 30) of the Trustees' answer in the state court proceeding, and are expressly admitted in the Attorneys' reply to said answer (R. 68).

Having induced those whom they represented to believe that the reorganization court would fix their fees for services in the prosecution of these claims, the Attorneys now repudiate their agreement. They claim that while the plan is binding upon the bondholders and stockholders whom they represented, it is not binding upon them!

The Trustees request that the order of the New York Court of Appeals be affirmed.

Respectfully submitted,

JOHN GERDES,
JAMES D. CARPENTER, JR.,
As Trustees of Reynolds Investing Company, Inc., Debtor, Pro Se, Respondents.

JOHN GERDES,
MARY-CHASE CLARK,
Of Counsel.

December 8, 1943.

APPENDIX.

State Statutes.

New York Decedent Estate Law.

§130. *Action by executor or administrator for negligence or wrongful act or default causing death of decedent.*

The executor or administrator duly appointed in this state, or in any other state, territory or district of the United States, or in any foreign country, of a decedent who has left him or her surviving a husband, wife, or next of kin, may maintain an action to recover damages for a wrongful act, neglect or default, by which the decedent's death was caused, against a natural person who, or a corporation which, would have been liable to an action in favor of the decedent by reason thereof if death had not ensued. Such an action must be commenced within two years after the decedent's death. When the husband, wife or next of kin, do not participate in the estate of decedent, under a will appointing an executor, other than such husband, wife or next of kin, who refuses to bring such action, then such husband, wife or next of kin shall be entitled to have an administrator appointed for the purpose of prosecuting such action for their benefit.

New York Judiciary Law, Sections 474 and 475.

§474. *Compensation of attorney or counsellor.*

The compensation of an attorney or counsellor for his services is governed by agreement, express or implied, which is not restrained by law. * * *

§475. *Attorney's lien in action, special or other proceeding.*

From the commencement of an action, special or other proceeding in any court or before any state or federal

department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien.

NEW YORK RULES OF CIVIL PRACTICE.

Rule 21. *Manner of service of papers to begin a proceeding.*

The provisions of the statutes and rules relating to the mode of personal service of a summons shall apply to the service of any process or other paper whereby a proceeding is begun in a court, or before an officer, except a proceeding to punish for contempt, unless other special provision for the service thereof is made by law or rule. Other papers in a proceeding shall be served in like manner as in an action.

Federal Statutes.

JUDICIAL CODE, SECTION 66

(28 U. S. C. A. 125).

SEC. 125. Suits against receiver. Every receiver or manager of any property appointed by any court of the United States may be sued in respect of any act or transaction of his in carrying on the business connected with such property, without the previous leave of the

court in which such receiver or manager was appointed: but such suit shall be subject to the general equity jurisdiction of the court in which such manager or receiver was appointed so far as the same may be necessary to the ends of justice.

FEDERAL BANKRUPTCY ACT.

SEC. 23. JURISDICTION OF UNITED STATES AND STATE COURTS.—a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67, and 70 of this Act.

SEC. 62. EXPENSES OF ADMINISTERING ESTATES; UNAUTHORIZED SHARING OF FEES; WITHHOLDING ALLOWANCES. a. The actual and necessary costs and expenses incurred by officers in the administration of estates shall, except where other provisions are made for their payment, be reported in detail, under oath, and examined and approved or disapproved by the court. If approved, they shall be paid or allowed out of the estates in which they were incurred. * * *

c. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, rendering services in a proceeding under this Act or in connection with such proceeding, shall not in any form or guise share or agree to share his compensation for such services with any person not contributing thereto, or share or agree to share in the compensation of any person rendering services in a proceeding under this Act or in connection with such proceeding, to which services he has not contributed: *Provided, however,* That an attorney-at-law may share such compensation with a law partner or with a forwarding attorney-at-law, and may share in the compensation of a law partner.

d. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, seeking compensation for services rendered by him in a proceeding under this Act or in connection with such proceeding, shall file with the court his petition setting forth the value and extent of the services rendered, the amount requested and what allowances, if any, have theretofore been made to him. Such petition shall be accompanied by his affidavit stating whether an agreement or understanding exists between the petitioner and any other person for a division of compensation and, if so, the nature and particulars thereof. If satisfied that the petitioner has, in any form or guise, shared or agreed to share his compensation or in the compensation of any other person contrary to the provisions of this subdivision, the court shall withhold all compensation from such petitioner.

SEC. 64. a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the filing fees paid by creditors in involuntary cases;

where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge, the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, as the court may allow; (2) wages, not to exceed $600, to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) where the confirmation of an arrangement or wage-earner plan or the bankrupt's discharge has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors, or, where through the efforts and at the cost and expense of one or more creditors, evidence shall have been adduced resulting in the conviction of any person of an offense under this title, the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside, or in adducing such evidence; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: Provided, That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the Court: And

provided further, That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States is entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State law; Provided, however, That such priority for rent to a landlord shall be restricted to the rent which is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.

b. Debts contracted while a discharge is in force or after the confirmation of an arrangement shall, in the event of a revocation of the discharge or setting aside of the confirmation, have priority and be paid in full in advance of the payment of the debts which were provable in the bankruptcy or arrangement proceeding, as the case may be.

SEC. 67. * * *

b. The provisions of section 96 of this title to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under chapter 10, 11, 12, or 13 of this title, by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to

be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

SEC. 111. Where not inconsistent with the provisions of this chapter, the court in which a petition is filed shall, for the purposes of this chapter, have exclusive jurisdiction of the debtor and its property, wherever located.

SEC. 116. Upon the approval of a petition, the judge may, in addition to the jurisdiction, powers, and duties hereinabove and elsewhere in this chapter conferred and imposed upon him and the court— * * *

(2) authorize a receiver, trustee, or debtor in possession, upon such notice as the judge may prescribe and upon cause shown, to issue certificates of indebtedness for cash, property, or other consideration approved by the judge, upon such terms and conditions and with such security and priority in payment over existing obligations, secured or unsecured, as in the particular case may be equitable; * * *

SEC. 148. Until otherwise ordered by the judge, an order approving a petition shall operate as a stay of a prior pending bankruptcy, mortgage foreclosure, or equity receivership proceeding, and of any act or other proceeding to enforce a lien against the debtor's property.

SEC. 157. An attorney appointed to represent a trustee under this chapter shall also be a disinterested person: Provided, however, That for any specified purposes other than to represent a trustee in conducting the proceeding under this chapter the trustee may, with the approval of the judge, employ an attorney who is not disinterested.

SEC. 206. The debtor, the indenture trustees, and any creditor or stockholder of the debtor shall have the right to be heard on all matters arising in a proceeding under this chapter. * * *

Federal Bankruptcy Act.

SEC. 216. A plan of reorganization under this chapter—

(1) shall include in respect to creditors generally or some class of them, secured or unsecured, and may include in respect to stockholders generally or some class of them, provisions altering or modifying their rights, either through the issuance of new securities of any character or otherwise;

(2) may deal with all or any part of the property of the debtor;

(3) shall provide for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge;

(4) may provide for the rejection of any executory contract except contracts in the public authority;

(5) shall specify what claims, if any, are to be paid in cash in full;

(6) shall specify the creditors or stockholders or any class of them not to be affected by the plan and the provisions, if any, with respect to them;

(7) shall provide for any class of creditors which is affected by and does not accept the plan by the two-thirds majority in amount required under this chapter, adequate protection for the realization by them of the value of their claims against the property dealt with by the plan and affected by such claims, either as provided in the plan or in the order confirming the plan, (a) by the transfer or sale, or by the retention by the debtor, of such property subject to such claims; or (b) by a sale of such property, free of such claims, at not less than a fair upset price, and the transfer of such claims to the proceeds of such sale; or (c) by appraisal and payment in cash of the value of such claims; or (d) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection;

(8) shall provide for any class of stockholders which is affected by the plan and does not accept the plan by the majority of the stock required under this chapter, adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with by the plan, either as provided in the plan or in the order confirming the plan, (a) by the sale of such property at not less than a fair upset price; or (b) by appraisal and payment in cash of the value of their stock; or (c) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection: Provided, however, That such protection shall not be required if the judge shall determine that the debtor is insolvent;

(9) may include, where any indebtedness is created or extended under the plan for a period of more than five years, provisions for the retirement of such indebtedness by stated or determinable payments out of a sinking fund or otherwise, (a) if secured, within the expected useful life of the security therefor, or (b) if unsecured, or if the expected useful life of the security is not fairly ascertainable, then within a specified reasonable time, not to exceed forty years;

(10) shall provide adequate means for the execution of the plan, which may include: the retention by the debtor of all or any part of its property; the sale or transfer of all or any part of its property to one or more other corporations theretofore organized or thereafter to be organized; the merger or consolidation of the debtor with one or more other corporations; the sale of all or any part of its property, either subject to or free from any lien, at not less than a fair upset price and the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein; the satisfaction or modification of liens; the cancelation or modification of indentures or of other

similar instruments; the curing or waiver of defaults; the extension of maturity dates and changes in interest rates and other terms of outstanding securities; the amendment of the charter of the debtor; the issuance of securities of the debtor or such other corporations for cash, for property, in exchange for existing securities, in satisfaction of claims or stock or for other appropriate purposes;

(11) shall include provisions which are equitable, compatible with the interests of creditors and stockholders, and consistent with public policy, with respect to the manner of selection of the persons who are to be directors, officers, or voting trustees, if any, upon the consummation of the plan, and their respective successors;

(12) shall provide for the inclusion in the charter of the debtor, or any corporation organized or to be organized for the purpose of carrying out the plan, of—

(a) provisions prohibiting the debtor or such corporation from issuing non-voting stock, and providing, as to the several classes of securities of the debtor or of such corporation possessing voting power, for the fair and equitable distribution of such power among such classes, including, in the case of any class of stock having a preference over other stock with respect to dividends, adequate provisions for the election of directors representing such preferred class in the event of default in the payment of such dividends; and

(b) (1) provisions which are fair and equitable and in accordance with sound business and accounting practice, with respect to the terms, position, rights, and privileges of the several classes of securities of the debtor or of such corporation, including, without limiting the generality of the foregoing, provisions with respect to the issuance, acquisition, purchase, retirement or redemption of any such securities, and the declaration and payment of dividends thereon; and (2) in the case of a

debtor whose indebtedness, liquidated as to amount and not contingent as to liability, is $250,000 or over, provisions with respect to the making, not less than once annually, of periodic reports to security holders which shall include profit and loss statements and balance sheets prepared in accordance with sound business and accounting practice;

(13) may include provisions for the settlement or adjustment of claims belonging to the debtor or to the estate; and shall provide, as to such claims not settled or adjusted in the plan, for their retention and enforcement by the trustee or, if the debtor has been continued in possession, by an examiner appointed for that purpose; and

(14) may include any other appropriate provisions not inconsistent with the provisions of this chapter.

SEC. 221. THE JUDGE SHALL CONFIRM A PLAN IF SATISFIED THAT—* * *

(4) all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge; * * *

SEC. 226. The property dealt with by the plan, when transferred by the trustee to the debtor or other corporation or corporations provided for by the plan, or when transferred by the debtor in possession to such other corporation or corporations, or when retained by the debtor in possession, as the case may be, shall be free and clear of all claims and interests of the debtor, creditors, and stockholders, except such claims and interests as may otherwise be provided for in the plan or in the

order confirming the plan or in the order directing or authorizing the transfer or retention of such property.

SEC. 227. The court may direct the debtor, its trustee, any mortgagees, indenture trustees, and other necessary parties to execute and deliver or to join in the execution and delivery of such instruments as may be requisite to effect a retention or transfer of property dealt with by a plan which has been confirmed, and to perform such other acts, including the satisfaction of liens, as the court may deem necessary for the consummation of the plan.

SEC. 241. The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceeding under this chapter—

(1) by a referee;

(2) by a special master;

(3) by the trustee and other officers, and the attorneys for any of them;

(4) by the attorney for the debtor; and

(5) by the attorney for the petitioning creditors.

Such compensation of referees and trustees shall not be governed by sections 40 and 48 of this Act. * * *

SEC. 247. The judge shall fix a time of hearing for the consideration of applications for allowances, of which hearing notice shall be given to the applicants, the trustee, the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate, except that, in the case of allowances for services and reimbursement in a superseded bankruptcy proceeding, notice need be given only to the applicants, the debtor, the trustee, and the unsecured creditors, and may be given to such other classes of creditors or other persons as the judge

may designate. In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that bankruptcy be proceeded with, notice of the hearing to consider allowances need not be given to stockholders.

SEC. 249. Any persons seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter, shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior consent or subsequent approval of the judge, been otherwise acquired or transferred.

SEC. 257. The trustee appointed under this chapter, upon his qualification, or if a debtor is continued in possession, the debtor, shall become vested with the rights, if any, of such prior receiver or trustee in such property and with the right to the immediate possession thereof. The trustee or debtor in possession shall also have the right to immediate possession of all property of the debtor in the possession of a trustee under a trust deed or a mortgagee under a mortgage.

SEC. 276 c. The provisions of sections 77A and 77B of chapter VIII, as amended, of the Act entitled "An Act to establish a uniform system of bankruptcy throughout

the United States", approved July 1, 1898, shall continue in full force and effect with respect to proceedings pending under those sections upon the effective date of this amendatory Act, except that—

(1) if the petition in such proceedings was approved within three months prior to the effective date of this amendatory Act, the provisions of this chapter shall apply in their entirety to such proceedings;

General Orders in Bankruptcy.

Order 44.

APPOINTMENT OF ATTORNEYS.

No attorney for a receiver, trustee or debtor in possession shall be appointed except upon the order of the court, which shall be granted only upon the verified petition of the receiver, trustee or debtor in possession, stating the name of the counsel whom he wishes to employ, the reasons for his selection, the professional services he is to render, the necessity for employing counsel at all, and to the best of the petitioner's knowledge all of the attorney's connections with the bankrupt or debtor, the creditors or any other party in interest, and their respective attorneys. If satisfied that the attorney represents no interest adverse to the receiver, the trustee, or the estate in the matters upon which he is to be engaged, and that his employment would be to the best interests of the estate, the court may authorize his employment, and such employment shall be for specific purposes unless the court is satisfied that the case is one justifying a general retainer. If without disclosure any attorney acting for a receiver or trustee or debtor in possession shall have represented any interest adverse to the receiver, trustee, creditors or stockholders in any matter upon which he is employed for such receiver, trustee, or debtor in possession, the court may deny the allowance of any fee to such attorney, or the reimbursement of his expenses, or both, and may also deny any allowance to the receiver or trustee if it shall appear that he failed to make diligent inquiry into the connections of said attorney. * * *

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In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 183

B. H. INNESS BROWN, DAVID PAINE, ETHELBERT WARFIELD, ET AL., PETITIONERS

v.

JOHN GERDES AND JAMES D. CARPENTER, JR., TRUSTEES OF REYNOLDS INVESTING CO., INC., DEBTOR

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE

This controversy, which comes here from the Court of Appeals of the State of New York, arose in the course of the administration of the assets of the Reynolds Investing Company, Inc., a debtor in a proceeding for corporate reorganization under the Bankruptcy Act pending in the United States District Court for the District of New Jersey. Because of the substantial public investor interest in the debtor, the Securities and Exchange Commission has participated in the federal reorganization proceeding upon the re-

quest of the United States District Judge pursuant to Sec. 208 of Chapter X of the Bankruptcy Act (11 U. S. C. 608). In the proceedings before the New York Court of Appeals, the Commission filed a brief *amicus curiae* pursuant to permission granted by that Court. This brief is submitted by the Securities and Exchange Commission as *amicus curiae* in support of the respondents.

OPINIONS BELOW

The opinions of the Special Terms of the New York Supreme Court (R. 98, 109) were not officially reported, but one of the opinions (R. 98) has been published in 33 N. Y. Supp. (2d) 949. The Appellate Division, First Department, affirmed without opinion (264 App. Div. 852; R. 118–119). The opinion of the New York Court of Appeals (R. 124–129), reversing the Special Term and the Appellate Division, is reported in 290 N. Y. 468.

JURISDICTION

The judgment of the New York Court of Appeals was entered April 22, 1943 (R. 129–130). A motion for reargument was denied on May 27, 1943 (R. 130–131). A petition for a writ of certiorari was filed July 20, 1943, and granted October 11, 1943 (R. 132). Jurisdiction of this Court is invoked under Sec. 237 (b) of the Judicial Code (28 U. S. C. 344 (b)).

QUESTION PRESENTED

The United States District Court in a proceeding for reorganization under the Bankruptcy Act appointed attorneys, who represented the principal security holders' committees in the proceeding, to institute suits in the state courts of New York against former officers of the debtor on causes of action in favor of the debtor's estate.

The principal question is whether the attorneys were entitled to have their fees for conducting the state court litigation fixed by the state courts under Sec. 475 of the New York Judiciary Law, or whether they must look to the reorganization court for their fees.

STATUTES INVOLVED

The pertinent provisions of statutes involved in this case are set forth in the Appendix, *infra*, pp. 37–46.

STATEMENT

Despite differences between the statements of facts in the briefs of petitioners and respondents, it is believed that those statements together form a sufficient factual basis for an understanding of the Commission's views; accordingly, the facts will not be restated. The petitioners will be referred to herein as the Attorneys and the respondents as the Trustees.

SUMMARY OF ARGUMENT

Under Chapter X of the Bankruptcy Act, Congress has preempted for the federal reorganiza-

tion courts broad power to supervise and fix administrative costs and expenses and to award reasonable compensation for services rendered in reorganization proceedings (U. S. Const., Art. I, Sec. 8, clause 4; Bankruptcy Act, Secs. 62d, 216 (3), 221 (4), 241–50; 11 U. S. C. 102 (d), 616 (3), 621 (4), 641–50). Such compensation includes the fees of attorneys appointed by the reorganization court to collect assets for the estate by pursuing causes of action in other courts. *Watkins* v. *Sedberry,* 261 U. S. 571; *W. J. Davidson & Co.* v. *Friedman,* 140 Fed. 853 (C. C. A. 6, 1906). When a state court undertakes to fix the fees of attorneys appointed by a reorganization court, the result is a clear conflict with the congressional intention to give the federal reorganization courts complete control over the proceeding for the protection of public investors.

In this case the reorganization court did not surrender its power to fix the Attorneys' fees. The plan of reorganization, the order of confirmation and the acts of the reorganization court and the Trustees clearly manifested a determination on the part of the court to retain exclusive jurisdiction over those fees. The cases relied upon by the Attorneys to show an implied relinquishment of the reorganization court's control over their fees (*Sherman* v. *Buckley,* 119 F. (2d) 280 (C. C. A. 2, 1941), certiorari denied, 314 U. S. 657; *In re Cup Craft Paper Corporation,* 40 F. Supp. 927 (S. D. N. Y., 1941), affirmed *sub nom.*

New York Credit Men's Assn. v. *Schlesinger*, 126 F. (2d) 472 (C. C. A. 2)) concern attorneys who had been retained by bankrupts prior to the institution of bankruptcy proceedings and whose statutory liens had attached prior to the proceedings, and are thus clearly distinguishable from the instant case wherein the Attorneys were initially appointed by the reorganization court.

Properly construed, Section 475 of the New York Judiciary Law does not purport to regulate the fees of attorneys appointed by a federal reorganization court. The Attorneys were officers of the reorganization court and by their appointment impliedly agreed, and became bound, to look to that court alone for their compensation.

The decision of the New York Court of Appeals correctly held that the Attorneys should be remitted to the reorganization court for the determination and allowance of their fees, and that decision should be affirmed by this Court.

ARGUMENT

I

ALLOWANCE OF COMPENSATION TO ATTORNEYS APPOINTED IN A REORGANIZATION PROCEEDING UNDER THE BANKRUPTCY ACT TO PROSECUTE CAUSES OF ACTION ON BEHALF OF THE ESTATE IS AN ADMINISTRATIVE MATTER EXCLUSIVELY WITHIN THE JURISDICTION OF THE UNITED STATES DISTRICT COURT ENTERTAINING THE PROCEEDING

The question whether attorneys appointed by a federal reorganization court to prosecute causes

of action on behalf of the debtor's estate may have the value of their services to the estate fixed by state courts must be determined by considering whether Congress, in the reorganization provisions of the Bankruptcy Act, has exercised its paramount bankruptcy power in a manner precluding resort to state procedures for the allowance of fees to attorneys who conduct litigation in the state courts. Constitution of the United States, Art. I, Sec. 8, clause 4. See *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478, 483; *Gross* v. *Irving Trust Co.*, 289 U. S. 342, 344; *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 739. It is our view that in its comprehensive system of bankruptcy administration Congress has preempted for the federal reorganization courts the power to supervise costs and expenses and to award reasonable compensation for services rendered in reorganization proceedings.

The power of reorganization courts over fees of persons rendering services to debtors' estates in reorganization is an essential element of the entire bankruptcy system. It gives the bankruptcy court control over one of the most important aspects of the proceeding—the maintaining of a proper balance between fair remuneration to the officers who administer the reorganization proceeding and limitation upon the total costs of administration so that resort to the Act does not

become unduly burdensome.[1] One of the controlling reasons for the enactment of the bankruptcy reorganization statutes to supplant state and federal equity procedures was the desire to reduce the costs of corporate reorganization to creditors and stockholders. *Callaghan* v. *Reconstruction Finance Corporation*, 297 U. S. 464, 468–469. In addition, Congress has recognized that a reorganization proceeding is not ordinary litigation between private parties, but normally involves the rights and interests of numerous public investors, many of whom are unrepresented or inadequately represented in the proceeding. The statutory provisions regulating costs and expenses of the reorganization are therefore designed to encourage wider participation by security holders and to establish safeguards assuring loyal and disinterested representation. *Cf. Securities and Exchange Commission* v. *U. S. Realty & Improvement Co.*, 310 U. S. 434.

The power necessary to effectuate these reorganization purposes is found in various provisions of the Bankruptcy Act. Article XIII

[1] Thus, in corporate reorganization proceedings it is customary to defer final allowances until the consummation of the proceedings in order that the aggregate amount allowed may be measured by the success of the proceedings and the estate's ability to pay. *In re Keystone Realty Holding Co.*, 117 F. (2d) 1003 (C. C. A. 3, 1941); *In re Prudence Bonds Corp.*, 106 F. (2d) 44 (C. C. A. 2, 1939).

of Chapter X[2] (Secs. 241–250, 11 U. S. C. 641–650) is exclusively devoted to "Compensation and Allowances." To insure that all allowances out of the estate will be reasonably related to the size of the estate and the success of the reorganization, Sec. 258 (11 U. S. C. 658) effects centralized control over all administrative fees and expenses by providing that allowances for services rendered in state or federal court proceedings which are supplanted by reorganization proceedings must be fixed by the reorganization court

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[2] We do not refer to any of the provisions of former Sec. 77B of the Bankruptcy Act (11 U. S. C. 207) at this point for two reasons:

(1) The provisions of Sec. 77B, while not as detailed, indicate just as clearly as do the provisions of Chapter X that control over the allowance of fees must reside in the reorganization court.

(2) The provisions of Chapter X apply in their entirety to the corporate reorganization proceeding involved in this case. That proceeding was instituted on May 18, 1938 (R. 55), shortly before the enactment of Chapter X on June 22, 1938. However, the petition was not approved until January 19, 1939 (R. 56), some time after the effective date of Chapter X (September 22, 1938). Sec. 276c (1) of Chapter X (11 U. S. C. 676 (c) (1)) provides that if a petition under Sec. 77B is approved within three months prior to the effective date of Chapter X, the provisions of Chapter X shall apply in their entirety to the proceedings. Since the petition in this case was approved *subsequent* to the effective date of the amendatory Act, there can be no question that Chapter X is completely applicable. *Cf. In re Old Algiers*, 100 F. (2d) 374 (C. C. A. 2, 1938). This was fully recognized at the time the petition was approved, as shown by the order of approval (R. 55–61).

rather than by the court supervising the prior proceeding. See *In re Keystone Realty Holding Co.*, 117 F. (2d) 1003, 1006 (C. C. A. 3, 1941); *cf. Gross* v. *Irving Trust Co.*, 289 U. S. 342.

Allowances may be made only after hearing upon notice to "the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate". (Sec. 247, 11 U. S. C. 647.) At such hearings interested parties enjoy the statutory right to be heard (Sec. 206; 11 U. S. C. 606), which includes the right to appeal. *In re Keystone Realty Holding Co.*, 117 F. (2d) 1003 (C. C. A. 3, 1941).

The highest standards of fiduciary conduct are exacted of attorneys performing services for the reorganization estate. In seeking compensation under Chapter X they must file with the court a statement under oath showing claims against or stock of the debtor which have been acquired or transferred by them after the commencement of the proceeding. No compensation may be allowed to any attorney who, after assuming to act in a fiduciary capacity in the proceedings, has purchased or sold claims against or stock of the debtor. (Sec. 249, 11 U. S. C. 649; *In re Reynolds Investing Co., Inc.*, 130 F. (2d) 60 (C. C. A. 3, 1942.) The attorney seeking compensation must advise the district court by affidavit whether he has any agreement with any other person for a

division of his compensation. (See. 62d, 11 U. S. C. 102 (d).) He is precluded from making any agreement with a party in interest fixing the amount of his fee. (Act of August 25, 1937, c. 777, 50 Stat. 810, 28 U. S. C. 572a.)

Finally, the court's control over compensation is expressed in those provisions relating to the central purpose of reorganization—confirmation and consummation of a plan. This appears from Secs. 216 (3) and 221 (4). Section 216 prescribes the contents of any plan of reorganization and Subdivision 3 of that section requires the plan to "provide for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge." Sec. 221 provides that the judge shall confirm a plan if he is satisfied that "all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge." The plan of reorganization and the order of confirmation in this case contain appropriate provisions pursuant to these statutory mandates. See pp. 17–20, *infra*.

To implement still further the control of the bankruptcy court over fees and expenses, the General Orders in Bankruptcy promulgated by this Court provide that no attorney for a trustee shall be appointed except upon the order of the court (General Order 44). The bankruptcy court must be satisfied that the proposed appointee does not represent an interest adverse to the estate with respect to the matters upon which he is to be engaged; if such an interest remains undisclosed until after the appointment, the bankruptcy court is empowered to deny any allowance to the attorney (*ibid.; cf. Woods* v. *City National Bank & Trust Co. of Chicago*, 312 U. S. 262). General Order 44 and former General Order 42 (the equivalent of present Sec. 62 (d)) have been applied to the appointment and fees of attorneys retained to handle matters for the trustees in other states. *Albers* v. *Dickinson*, 127 F. (2d) 957, 961 (C. C. A. 8, 1942).

The compensation of attorneys appointed by a bankruptcy court to collect assets for the estate by pursuing causes of action in other courts is clearly an expense of the administration of the estate. See *Watkins* v. *Sedberry*, 261 U. S. 571; *W. J. Davidson & Co.* v. *Friedman*, 140 Fed. 853 (C. C. A. 6, 1906).[3] Accordingly, the foregoing

[3] The prosecution of causes of action like those conducted by the Attorneys in this case is an integral part of the administration of a Chapter X proceeding. One of the primary reasons for requiring the appointment of a disinterested

rules are applicable to the determination of such compensation.

When a state court undertakes to fix the fees of attorneys appointed by a bankruptcy court, as the lower New York courts did in this case, there results an inevitable collision with the clear intendment of the Bankruptcy Act. If a state court were allowed to fix the compensation of such attorneys, the reorganization court's centralized control over the proceeding before if would be dissipated, and the protection which Congress intended to accord to public investors would be denied. By the same token, if a state statute

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trustee in cases in which a substantial public investor interest exists (Sec. 156; 11 U. S. C. 556), is to assure the disclosure and pursuit of corporate assets in the form of claims against directors, officers, and others who may have misused corporate control for their personal benefit. See S. E. C. Report on Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees, Part VIII, page 337. Thus, Sec. 167 (3), 11 U. S. C. 567 (3), requires the disinterested trustee to report to the court any fraud, misconduct, mismanagement, or irregularities disclosed by his investigation and the availability of any causes of action to the estate. This provision "insures prosecution of all causes of action." S. Rep. No. 1916, 75th Cong., 3d sess. (1938), page 29. So important is this aspect of the administration of the estate that Sec. 216 (13), 11 U. S. C. 616 (13), makes it mandatory for the plan to provide for the retention and continued enforcement by the disinterested trustee of all claims not yet settled or adjusted. Pursuant to this requirement, the state court litigation in the present case continued even after consummation of the reorganization plan (R. 52–53).

were to be construed to authorize a determination of such fees, it would be unconstitutional to that extent.

> The States cannot, in the exercise of control over local laws and practice, vest state courts with power to violate the supreme law of the land. The Constitution grants Congress exclusive power to regulate bankruptcy and under this power Congress can limit the jurisdiction which courts, state or federal, can exercise over the person and property of a debtor who duly invokes the bankruptcy law. If Congress has vested in the bankruptcy courts exclusive jurisdiction over farmer-debtors and their property, and has by its Act withdrawn from all other courts all power under any circumstances to maintain and enforce foreclosure proceedings against them, its Act is the supreme law of the land which all courts—state and federal—must observe. [*Kalb* v. *Feuerstein*, 308 U. S. 433, 439.]

See also *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734; *Gross* v. *Irving Trust Co.*, 289 U. S. 342; *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478.

It should be noted that a holding that Sec. 475 of the New York Judiciary Law, involved in this case, may not constitutionally operate to permit state determination of the amount of fees in this situation will not materially restrict the scope of

operation of that section.[4] The Attorneys' brief incorrectly conveys the impression that Sec. 475 provides a complete and customary machinery for the determination of the compensation of attorneys who prosecute causes of action in the courts of New York. On the contrary, as we shall show, resort to Sec. 475 is the exception, rather than the rule; resort to Sec. 475 is by no means closely related to the prosecution of the principal action in the New York courts; and Sec. 475 is available in only a small number of the situations covered by the fee allowance provisions of the Bankruptcy Act.

Section 475 is not, as the Attorneys have sought to imply, a normal procedure by which attorneys obtain their compensation for conducting litigation. It exists "for the protection of attorneys against the knavery of their clients." *In re Maggio's Estate*, 169 Misc. 1039 (Surr. Ct., N. Y. Co. 1938). Consequently, court proceedings to enforce the charging lien are instituted at the option of the attorney only when the conduct of the client makes them necessary. In most instances, "knavery" is absent and no proceedings are required.

Furthermore, these proceedings are not necessarily a part of the primary litigation; they may

[4] As we point out further in Point III, *infra*, Sec. 475, when read with Sec. 474, does not permit determination by the state court of the amount of fees under the contract here involved.

be instituted as special proceedings apart from the main action. See *Smith* v. *First National Bank of Albany*, 103 Misc. 274, 279 (Sup. Ct., Special Term, 1917), modified in 184 App. Div. 719 (App. Div. 3d Dept., 1918); *In re Jacobs*, 169 Misc. 893 (Sup. Ct. Special Term, 1938). They need not be brought before the judge who presided at the trial, nor even before the same court. For example, proceedings under Section 475 have been instituted in the Surrogate's Court to enforce a lien for services rendered in the United States Customs Court. See *In re Levine's Estate*, 154 Misc. 700 (Surr. Ct., N. Y. Co., 1935). Many times the proceedings are utilized not to obtain determination of the value of the services, but merely to collect fees specified by retainers.

The scope of Section 475 is much narrower than the allowance provisions of the Bankruptcy Act. Section 475 cannot be used where the action involved does not result in a recovery or does not seek a judgment for money or money's worth. See *Davidson* v. *American Blower Co.*, 245 Fed. 773 (N. D. N. Y., 1917). Thus, if attorneys appointed by a bankruptcy court are unsuccessful in a state court action to recover a money judgment, or if the retainer is to defend the estate, they have no alternative but to resort to the bankruptcy court for allowances. Moreover, the provisions of Section 475 are available only to

attorneys of record. See *Matter of Sebrina* 238 App. Div. 281 (App. Div., 4th Dept., 1933). Thus, other counsel, expert witnesses, accountants, the trustee, and any others who rendered services to the debtor estate in connection with the state court litigation would in any event be compelled to return to the bankruptcy court for their compensation. The use of Section 475 by the attorney of record would, therefore, result in division of responsibility between two courts for determination of the cost of a single litigation and would consequently dissipate effective control over this expense.

It is clear, therefore, that the enforcement feature of Section 475 is neither a mandatory nor an adequate substitute for the extensive compensation machinery provided in the Bankruptcy Act. The salient fact is that no machinery is furnished either in the form of state statute or state court procedure for safeguarding public investor interests. The state court in such a case has neither the information nor the statutory guides necessary to coordinate its decision with the needs of the debtor and its security holders or with the final results to be achieved in the reorganization proceeding.[5] See *In re Keystone*

[5] An emphatic illustration is furnished in this case. At the time the state court was fixing the Attorneys' lien at $100,000 (excluding interest) for securing judgments in Cause of Action #1 (R. 7, 113), the Trustees were applying to the reorganization court for authority to settle the judgments for $150,000 (R. 93).

Realty Holding Co., 117 F. (2d) 1003 (C. C. A. 3, 1941), *supra*, and cases cited.

We submit, therefore, that the state statute may not be permitted to operate in this situation in a manner inconsistent with the paramount jurisdiction of the reorganization court over fees and expenses.

II

THE UNITED STATES DISTRICT COURT HAS NOT SURRENDERED ITS EXCLUSIVE JURISDICTION TO DETERMINE THE FEES TO BE ALLOWED THE ATTORNEYS

The federal reorganization court did nothing in this case which can be construed as a surrender to the state courts of jurisdiction over the Attorneys' fees. On the contrary, the federal court repeatedly made clear that it retained such jurisdiction.

The plan of reorganization consummated in the proceeding specifically dealt with the state court actions and with the payment of compensation and expenses in connection with those actions. Article XI of the plan is as follows (R. 52–53):

> XI. RESERVATION OF CAIMS
>
> All claims in favor of the Debtor or of the Debtor's estate not settled or adjusted in the reorganization proceedings, or in the plan, or in connection with the consummation of the plan, shall be retained and enforced by the Trustees. The Company

shall cooperate with and assist the Trustees in every way in the prosecution and collection of such claims.

The Trustees shall have full power to prosecute pending actions and proceedings involving such claims, and to bring additional actions or proceedings in the courts of any jurisdiction. They shall also have full power to employ, retain, or displace, attorneys or counsel representing them in any action or proceeding, whether such action or proceeding be pending at the time of the consummation of the plan or not. They shall not, however, have any power to discontinue, compromise or settle any action or proceeding without the express approval of the Court.

The Court will retain continuing jurisdiction over such claims and the prosecution thereof, and over the Company, its books, records and papers, and the Trustees, in connection therewith, after the final decree in the reorganization proceedings. *The Court will from time to time fix the reasonable compensation to be paid to the Trustees, and their attorneys or counsel, for services in the prosecution of such claims, and the Company shall assume and pay the amount of such compensation as well as all other expenses incurred or paid by the Trustees in the prosecution, collection, or other disposition of the claims.* If the value of the portfolio of the Company shall, at any time prior to a complete and final adjustment on the merits of all of the claims reserved to the Trustees, be $300,000

or less, the assets of the Company shall not be further depleted by purchases or redemptions of debentures or shares of preferred stock without order of the Court after a hearing upon notice to the Trustees.[6] In such order the Court will specify the financial arrangements to be made by the Company for the payment of all expenses then already incurred in connection with the claims as well as such other expenses as may reasonably be necessary in the further prosecution thereof.

The net proceeds ultimately resulting from the prosecution or other disposition of the claims will be paid to the Company. [Italics supplied.]

In conformity with Section 221 (4) (11 U. S. C. 621 (4)) the order confirming the plan (R. 62–67) recites that the court is satisfied that "all payments made or promised by the debtor, or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge" (R. 63). The same order further pro-

[6] This reservation of at least $300,000 of assets to provide compensation for the Attorneys' claims and other expenses emphasizes the federal court's intention to retain complete control.

vides that "the debtor shall pay all the costs and expenses of administration as shall hereafter be approved by the Judge after hearing upon notice as provided in Sections 62d and 247 of the Bankruptcy Act, and no other sums shall be paid by the debtor or by any other person, for services and for costs and expenses in the proceeding or in connection therewith, or in connection with the plan or incident to the reorganization" (R. 66). As we point out below, *infra*, pp. 32–33, the Attorneys acquiesced in the terms of the plan and the order of confirmation.

Finally, the stipulation of July 9, 1941, signed by the Trustees and approved by the district court (R. 24–26), contains the following specific reservation of rights (R. 26):

> 7. Nothing herein shall constitute a waiver of the rights of petitioners or respondents to question the jurisdiction of the courts of the State of New York, or the United States District Court for the District of New Jersey, with respect to the determination of the existence, nature or extent of respondents' liens and the payment of their fees and disbursements in connection with the aforesaid litigation.

Upon the Attorneys' application to the New York court for the determination of the lien, the reorganization Trustees requested the state court to recognize the exclusive jurisdiction of the federal court (R. 31, 69–70, 72–73). After this request was denied, the Trustees participated no

further in the state court proceedings (R. 73). Thus, the federal court and its Trustees observed the orderly procedure recommended in *Gross* v. *Irving Trust Co.*, 289 U. S. 342, 345, where this Court stated:

> Nevertheless, due regard for comity—which means, in this connection, no more than judicial courtesy between the courts undertaking to deal with the same matter—would suggest that ordinarily the trustee in bankruptcy might well be instructed by the bankruptcy court, before taking final action, to request the state court to recognize the exclusive jurisdiction of the former * * *.

This was consistent with the purpose of the district court throughout the proceedings to retain the power to fix interim and final allowances for the services rendered by the Attorneys.

Despite this evidence of the district court's determination not to relinquish control over the fees of the Attorneys, it is contended (Pet. Br. 11–23) that surrender must be implied from the District Court's granting of permission to prosecute the suits in the state court.[7] Principal reliance is placed upon *Sherman* v. *Buckley*, 119 F. (2d) 280 (C. C. A. 2, 1941), certiorari denied, 314 U. S.

[7] The Attorneys' contention overlooks the ordinary rule that the surrender of a matter arising in the course of a bankruptcy proceeding cannot be implied, but must be absolute and specific to permit a state court to assume jurisdiction. See *Palmer* v. *Larchmont Manor Co.*, 284 N. Y. 288 (1940);

657; *In re Cup Craft Paper Corporation*, 40 F. Supp. 927 (S. D. N. Y., 1941), affirmed *sub nom. New York Credit Men's Assn.* v. *Schlesinger*, 126 F. (2d) 472 (C. C. A. 2); and *Cup Craft Paper Corp.* v. *Federal Paper Board Co.*, 262 App. Div. 91 (1941); affirmed 289 N. Y. 671 (1942). In these cases, however, the statutory liens had attached prior to the institution of the bankruptcy proceeding. The state court actions had been commenced by the bankrupts through the attorneys involved in the lien proceedings before the filing of the bankruptcy petitions, and all substantial services had been performed prior to the commencement of the bankruptcy proceedings.* Section 67b of the Bankruptcy Act (11 U. S. C. 107) specifically recognizes the validity of such liens for services rendered prior to bankruptcy and provides that they may be perfected subsequent to bankruptcy. See *In re Prudence Co.*, 96 F. (2d) 157, 160 (C. C. A. 2, 1938), certiorari denied, *sub nom. McGrath, et al.* v. *Davison*, 305 U. S. 616. In the present case, *the Attorneys were originally appointed by the federal reorganization court*, and went into the state court as officers of the federal court subject to the provisions of the

* It is true that the services of the attorneys in *Sherman* v. *Buckley* were not terminated until February 25, 1935, although the bankrupt was adjudicated on January 11, 1934. During this period, however, the attorneys continued to serve under their retainer from the bankrupt, and were never authorized by the bankruptcy court to act as attorneys for the trustee. Consequently, our argument concerning the attorneys in the *Prudence* case is equally applicable to this situation. See *infra*, pp. 24–25.

Bankruptcy Act with respect to compensation for their services. *In re Stemper*, 222 Fed. 690, 692 (D. Ariz., 1915); *In re Flaherty*, 295 Fed. 699, 700 (D. Mont., 1924).

We do not understand the *Buckley* case as intimating that the mere submission to another court of the prosecution of an action by appointees of a bankruptcy court constitutes a surrender of all control over the matter.[9] The circuit court of appeals recognized that jurisdiction is retained over such incidents as the settlement or discontinuance of the suit,[10] since these are bankruptcy matters within the exclusive jurisdiction of the bankruptcy court. Likewise, we

[9] In the *Buckley* case, upon which the *Cup Craft* case relied, the trustee voluntarily submitted to the state court procedure for substitution of attorneys in the action pending, suggested that the state court grant a charging lien to the displaced attorneys, made the motion upon which the state court fixed the lien, and acted under the order of the state court fixing the lien for five and one-half years. In other words, that case involved something more than the submission to the state court of the prosecution of a cause of action. It is therefore understandable that the circuit court of appeals viewed the permission granted to the state court in that case as necessarily involving "a consent to such incidents as the exercise of that court's jurisdiction might involve, among them that, as a condition upon the substitution of new attorneys, the charging lien of the displaced attorneys must be liquidated" (119 F. (2d) at 282).

[10] The court stated (119 F. (2d) at 282): "We need not, and we do not, hold therefore that if the trustee had brought Buckley & Buckley summarily into the bankruptcy court and insisted upon the liquidation of their lien, preparatory for example to a discontinuance or settlement of the action, they would have had any defence." See Bankruptcy Act, Sec. 27 (11 U. S. C. 50).

submit, the award of compensation to attorneys appointed by a court of bankruptcy, as distinguished from attorneys employed before bankruptcy by the bankrupt or debtor, is exclusively an administrative problem remaining with the court of appointment, and is not an automatic adjunct of the enforcement of the cause of action.

In *In re Prudence Company, Inc.*, 96 F. (2d) 157 (C. C. A. 2, 1938), certiorari denied *sub nom. McGrath, et al.* v. *Davison*, 305 U. S. 616, also relied on by the Attorneys, the suit was likewise instituted prior to reorganization by an attorney selected by the debtor. Instead of taking over the prosecution of the suit, the reorganization trustee elected to allow the suit to be continued by the debtor and its attorney. This course, the court found, enabled the trustee "to obtain the benefit of such judgment as the debtor might finally obtain without subjecting the estate to liability for past or future services of the attorney or for costs, in case the suit should fail." (96 F. (2d) at 159). Thus, while services were performed by the attorney subsequent to the reorganization petition, they were performed pursuant to the retainer with the debtor and not as court appointee. Nevertheless, when the suit had been successfully concluded, the attorney moved in the *reorganization court* for an order awarding him compensation in accordance with his retainer; he made no effort to enforce his charging lien in any other court. The case

merely reaffirms the conceded proposition that where a valid charging lien exists it will be enforced by the bankruptcy court and there is no occasion to seek its enforcement elsewhere. This is a far different matter from implying the surrender of the court's control over the fees of its appointees.

The Attorneys have devoted a whole point (Pet. Br., Point III, pp. 26–36) to an argument founded on a misunderstanding of the basis of the decision below and of the Trustees' position. The Attorneys assume that the decision rests on the grant in Chapter X to United States district courts of jurisdiction over plenary actions brought by trustees. They then argue that the reliance on this grant of jurisdiction in Chapter X is misplaced, because the trustees' Cause of Action No. 1 was brought while Sec. 77B was in effect, and under Sec. 77B the United States district courts had no equivalent power over plenary suits.

The Attorneys' argument is irrelevant, for they have misconceived the nature of the bankruptcy powers relied upon. The court below and the Trustees rely on the provisions of the Bankruptcy Act which permit the district court to control the causes of action *as assets of the estate*, and to control fee allowances for services in the collection of these assets. See *supra*, Point I. In

this respect the provisions of Sec. 77B were not materially different from those of Chapter X.

The Trustees' argument in no sense rests on the power of the district court over the causes of action as *justiciable controversies*. Accordingly, while it is true that there is a difference between Sec. 77B and Chapter X with respect to the judicial power of the district courts to adjudicate the causes of action, that difference in power is not material to the basis of the decision below or to the Trustees' argument.

Furthermore, as applied to the circumstances of this case, the district court in New Jersey would have no greater power under Chapter X to entertain suits against defendants in New York than it would have in Section 77B. While the point is irrelevant, the Attorneys have devoted so much space to the problem that, for the Court's convenience, we discuss in the following paragraphs the change wrought by Chapter X in the power of the district court to adjudicate causes of action in favor of the estate.

The change rests in the fact that Sec. 23 of the Bankruptcy Act (11 U. S. C. 46) is expressly made inapplicable to Chapter X, while it was applicable to Sec. 77B.[11] But the only conse-

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[11] Bankruptcy Act, Sec. 102 (11 U. S. C. 502); *Warder* v. *Brady*, 115 F. (2d) 89 (C. C. A. 4, 1940); see *In re Standard Gas & Electric Co.*, 119 F. (2d) 658 (C. C. A. 3, 1941); *Tilton* v. *Model Taxi Corp.*, 112 F. (2d) 86 (C. C. A. 2, 1940).

quence of this change is to add to the number of forums which may entertain plenary suits. Section 23 invests the United States district courts with jurisdiction to entertain controversies arising out of proceedings in bankruptcy between trustees and adverse claimants, but further provides that such plenary suits, as distinguished from summary proceedings in bankruptcy, may be brought only in the state or federal courts where the bankrupt might have brought or prosecuted them. The net effect of these provisions is that a plenary suit may be initiated in the federal courts only when the customary elements of federal jurisdiction exist, e. g., diversity of citizenship.

In declaring Section 23 expressly inapplicable, Chapter X has substituted the equity receivership rule that a receiver may sue in the federal court of his appointment without satisfying the ordinary requirements for federal jurisdiction. *White* v. *Ewing*, 159 U. S. 36, 39; *Krippendorf* v. *Hyde*, 110 U. S. 276. Thus, the only change wrought by Chapter X in this connection is to provide, as an additional forum, the federal district court in which the Chapter X proceedings are pending. *Cf. Grant* v. *Buckner*, 172 U. S. 232, 238; *Equitable Trust Co.* v. *Donney*, 24 F. (2d) 169, 171 (C. C. A. 7, 1928). In this forum the action is still plenary and not summary, service over the defendants must be acquired in the manner usual

to plenary suits, and the geographical rules as to service of process apply. See *Warder* v. *Brady*, 115 F. (2d) 89, 94 (C. C. A. 4, 1940). Since personal jurisdiction over the defendants could not be obtained in New Jersey, where the reorganization proceedings are pending, the causes of action involved here had to be instituted in a New York court, and the situation in this respect is precisely the same under Chapter X as under Sec. 77B.

The coincidental fact that a plenary suit is brought in the same federal court in which the reorganization is pending gives the judge presiding over the reorganization no greater control over the trial of the plenary action than he could exercise over the same suit in a state court. Thus, whether Sec. 77B or Chapter X be applied,[12] and whether the suit be brought in a state court or a federal court, the litigation itself is equally free from interference by the reorganization court. The court which is entertaining the suit has indisputable jurisdiction over the cause of action insofar as it is a "controversy" or a plenary suit. Only that court, for example, can pass upon the validity of service of process, determine the sufficiency of the pleadings, or award judgment. But these incidents of the plenary action are not to be confused, as the Attorneys have done, with mat-

[12] We have shown that the provisions of Chapter X are applicable in their entirety to these proceedings. (See *supra*, footnote 2, page 8.)

ters incident to the debtor's administration in reorganization. In the sense that these causes of action are assets of the debtor to be administered in the proceedings, they are subject to the control of the reorganization court. That court alone may decide whether actions should be brought, in which of the available forums they should be conducted, what attorneys should be retained to pursue them, whether and on what terms they should be settled or discontinued (see *supra*, footnote 5, p. 16), and what fees and expenses should be awarded to its appointees.

III

IT WAS AN IMPLIED TERM OF THE EMPLOYMENT OF THE ATTORNEYS THAT THEY WOULD LOOK TO THE REORGANIZATION COURT FOR ALLOWANCE AND PAYMENT OF THEIR CLAIM. ACCORDINGLY, SEC. 475, READ IN CONNECTION WITH SEC. 474, DOES NOT AUTHORIZE DETERMINATION OF SUCH CLAIM BY THE STATE COURT

We do not believe that Sec. 475, properly applied, conflicts with jurisdiction of the reorganization court, or that it compels an unconstitutional result in this case. The lien provided by Sec. 475 is designed to protect the agreement for compensation authorized by Sec. 474 of the New York Judiciary Law. The two sections must be considered together. They provide as follows:

§ 474. *Compensation of attorney or counsellor.*

The compensation of an attorney or

counsellor for his services is governed by agreement, express or implied, which is not restrained by law * * *.

§ 475. *Attorney's lien in action, special or other proceeding.*

From the commencement of an action, special or other proceeding in any court or before any state or federal department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien.

To determine what was the contract which Sec. 475 is designed to protect, it is necessary to consider the terms of the appointment of the Attorneys. The order authorizing them to bring the state court action does not specify the terms of the retainer. Those terms must, consequently, be implied from the circumstances, legal and factual, under which the services were authorized and rendered. The New York Court of Appeals

has found that "*both as a matter of law and as a matter of fact* the retainer of these attorneys was subject to the condition that the amount of any fees would be fixed by the United States District Court" (R. 128) [italics added]. The controlling statutory provisions of Chapter X, which in our view must be read into the contract,[13] and the facts of this case amply support this finding.

As we have pointed out, the prosecution of the state court actions was a part of the administration of the reorganization estate; and, under the provisions of the Bankruptcy Act, compensation for services in connection with such administration must be allowed by the bankruptcy court after compliance with procedural requirements as

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[13] This is not the only situation where statutory conditions have been implied as a matter of law in retainers authorized by Sec. 474. For example, Sec. 133 of the New York Decedent Estate Law provides that the reasonable expenses of actions for the wrongful death of a decedent may be fixed by the Surrogate. This has been held to empower the Surrogate to fix a reasonable fee for an attorney's services in prosecuting such an action in another court despite the express terms of the retainer between the attorney and the representative of the decedent's heirs. See *Matter of Meng*, 227 N. Y. 264 (1919); *Pantano* v. *Erie County Savings Bank of Buffalo*, 257 App. Div. 451 (4th Dept. 1939). Sometimes the fee is fixed by the New York Supreme Court because it has concurrent jurisdiction with the Surrogate over such matters. See *Matter of Atterbury*, 222 N. Y. 355 (1918). In citing cases of this character for the proposition that the fees may be fixed on a *quantum meruit* basis (Pet. Br. 14–15), the Attorneys have ignored the cited provision of the Decedent Estate Law.

to notice and hearing and filing of affidavits negativing the existence of possible disqualifications. *Supra*, pp. 9–10. General Order in Bankruptcy 44, which requires court authorization for the appointment of attorneys to represent trustees in any matter, clearly envisions that the compensation of the attorneys will be controlled by the bankruptcy court. We have pointed out that this order applies to employment of attorneys to prosecute claims on behalf of the estate. *Supra* p. 11. The district court's control is so complete that the trustee may not even adjust the attorneys' fees for such services by agreement. *In re Flaherty*, 295 Fed. 699 (D. Mont., 1924); *In re Stemper*, 222 Fed. 690 (D. Ariz., 1915). We believe that the conclusion is inescapable that it was an implied term of the agreement that the attorneys appointed by the federal court would look for their fees to the procedure specified in the statute governing their appointment.

This conclusion is borne out by the statutory provisions governing formulation and confirmation of the plan, which require provision for fees to be made in the plan and further require a finding of the court that the fees are reasonable or will be subject to the court's subsequent approval. *Supra* p. 10.

The statutory scheme was fully adhered to by the district court and the parties in this case. As we have shown, *supra* pp. 17–20, the plan and the

order of confirmation clearly reserved to the reorganization court the power to determine compensation for the prosecution of the causes of action. The Attorneys acquiesced in both the plan and the order. The Attorneys already had performed services in the state courts when the plan was filed and when it was confirmed. Yet they raised no objection to the plan or to the order of confirmation. This circumstance emphatically supports our view that the statutory scheme contemplating allowance of the Attorneys' fees by the reorganization court was an implied term of the agreement of employment."

Further confirmation for this view of the contract comes from the practice and custom in such situations. The cases dealing with similar situations have uniformly recognized that the compensation of attorneys appointed by a bankruptcy

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"In this case, unlike *Sherman* v. *Buckley* and the *Cup Craft* cases, there has been no breach of the agreement of employment by discharge of the attorneys. Petitioners (Pet. Br. 25) cite language of the New York *nisi prius* judge implying that there had been a discharge in this case, and then erroneously state that the New York Court of Appeals did not disturb this finding. On the contrary, the Court of Appeals said (R. 128):

"* * * the attorneys in both of these cases [*Sherman* v. *Buckley* and the *Cup Craft* cases] were discharged and not permitted to complete the services for which they had been employed under a single contract of contingent retainer, whereas the attorneys herein were permitted fully to perform the services for which they were appointed, namely to reduce the claims to judgment."

court to perform administrative services should be fixed by that court, even though the services consisted of prosecutions of actions in other courts. *Watkins* v. *Sedberry*, 261 U. S. 571; *In re Cheney*, 300 Fed. 465 (D. Mass., 1924); *In re Evans*, 117 Fed. 574 (E. D. N. C., 1902); *In re McKenna*, 137 Fed. 611 (N. D. N. Y., 1905); *In re J. M. Fiske & Co.*, 209 Fed. 982 (S. D. N. Y., 1913); *In re Stemper*, 222 Fed. 690 (D. Ariz., 1915); *In re Levinson*, 19 F. (2d) 253 (W. D. Wash., 1927); *Watters* v. *Hamilton Gas Co.*, 29 F. Supp. 436, 477 (S. D. W. Va., 1939). We know of no case other than the present one in which attorneys who were first appointed by the bankruptcy court have sought an allowance of fees elsewhere than in that court.

The crucial question here is not whether a lien exists, but rather which court may determine the fees. Since approval of the Attorneys' fees by the reorganization court was clearly a condition of the original authorization, we submit that the lien under Sec. 475 (even if available to the Attorneys) cannot be enforced in disregard of that condition. Sec. 475 does not authorize determination of the amount of attorneys' compensation by the state court if the parties' contract contemplates determination in some other manner. Thus clearly Sec. 475 could not be used to procure a determination of the amount of services in an amount greater than that contained in the agreement of retainer, no matter what the reason-

able value of the services might be. It has even been held in New York that there is no lien under Sec. 475 unless it was within the contemplation of the parties that the attorneys would be paid out of the proceeds of the recovery. In *Matter of Heinsheimer,* 214 N. Y. 361, 368 (1915), the court said:

> A charging lien cannot exist unless it is an element, express or implied, of the agreement that the lawyer is to be paid out of the fruits of the judgment.

Our view of the contract and the application of Sec. 475 thereto is supported by the approach taken by the New York Court of Appeals. That court said (R. 126–129):

> * * * since these attorneys were appointed by the court in this reorganization proceeding and nothing was said as to fees, the services of the attorneys were undertaken subject to all the provisions of the Bankruptcy Act with respect to the compensation for such services. * * * Under such circumstances, even if no exclusive jurisdiction had been given to the Federal court, the attorneys would in the normal course return to have their compensation fixed by the court by whom their appointment had been made. * * * It is unnecessary to consider whether it was within the power of the court to surrender this jurisdiction, since it would appear that both as a matter of law and as a matter of fact the retainer of these attorneys was subject to the condition that the amount

of any fees would be fixed by the United States District Court. * * * As already noted, in the case at bar the attorneys were appointed by the court pending the reorganization proceeding to perform services as agents and appointees of the court. The allowances for the attorneys were administration expenses covered by the allowance provisions of the Bankruptcy Act.

It follows that the orders appealed from should be reversed and the proceedings dismissed without costs.

CONCLUSION

For all of the above reasons, the judgment of the Court of Appeals for the State of New York should be affirmed.

Respectfully submitted,

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DECEMBER 1943.

APPENDIX

CONSTITUTION OF THE UNITED STATES (ARTICLE 1, SECTION 8, CL. 4)

The Congress shall have Power * * * To establish * * * uniform Laws on the subject of Bankruptcies throughout the United States; * * *.

STATUTES INVOLVED

JUDICIAL CODE, SECTION 256 (28 U. S. C. 371)

EXCLUSIVE JURISDICTION OF UNITED STATES COURTS

The jurisdiction vested in the courts of the United States in the cases and proceedings hereinafter mentioned, shall be exclusive of the courts of the several States.

* * * * *

Sixth. Of all matters and proceedings in bankruptcy.

BANKRUPTCY ACT

SEC. 23 (11 U. S. C. 46). JURISDICTION OF UNITED STATES AND STATE COURTS.—a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67, and 70 of this Act.

SEC. 27 (11 U. S. C. 50). COMPROMISES.—The receiver or trustee may, with the approval of the court, compromise any controversy arising in the administration of the estate upon such terms as he may deem for the best interest of the estate.

SEC. 62 (11 U. S. C. 102). EXPENSES OF ADMINISTERING ESTATES; UNAUTHORIZED SHARING OF FEES; WITHHOLDING ALLOWANCES.—

* * * * *

d. A custodian, receiver, or trustee or the attorney for any of them, or any other attorney, seeking compensation for services rendered by him in a proceeding under this Act or in connection with such proceeding, shall file with the court his petition setting forth the value and extent of the services rendered, the amount requested and what allowances, if any, have theretofore been made to him. Such petition shall be accompanied by his affidavit stating whether an agreement or understanding exists between the petitioner and any other person for a division of compensation and, if so, the nature and particulars thereof. If satisfied that the petitioner has, in any form or guise, shared or agreed to share his compensation or in the compensation of any other person contrary to the provisions of this subdivision, the court shall withhold all compensation from such petitioner.

SEC. 67 (11 U. S. C. 107). LIENS AND FRAUDULENT TRANSFERS.—

* * * * *

b. The provisions of section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the petition in bankruptcy or of the original petition under chapter X, XI, XII, or XIII of this Act, by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

SEC. 167 (11 U. S. C. 567). The trustee upon his appointment and qualification—

* * * * *

(3) shall report to the judge any facts ascertained by him pertaining to fraud, misconduct, mismanagement and irregularities, and to any causes of action available to the estate;

SEC. 206 (11 U. S. C. 606). The debtor, the indenture trustees, and any creditor or stockholder of the debtor shall have the right to be heard on all matters arising in a proceeding under this

chapter. The judge may, for cause shown, permit a labor union or employees' association, representative of employees of the debtor, to be heard on the economic soundness of the plan affecting the interests of the employees.

ARTICLE X—PROVISIONS OF PLAN

SEC. 216 (11 U. S. C. 616). A plan of reorganization under this chapter—

* * * * * *

(3) shall provide for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge;

* * * * * *

(13) may include provisions for the settlement or adjustment of claims belonging to the debtor or to the estate; and shall provide, as to such claims not settled or adjusted in the plan, for their retention and enforcement by the trustee or, if the debtor has been continued in possession, by an examiner appointed for that purpose; * * *

ARTICLE XI—CONFIRMATION AND CONSUMMATION OF PLAN

SEC. 221 (11 U. S. C. 621). The judge shall confirm a plan if satisfied that—

* * * * * *

(4) all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the

reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge; * * *

ARTICLE XIII—COMPENSATION AND ALLOWANCES

SEC. 241 (11 U. S. C. 641). The judge may allow reimbursement for proper costs and expenses incurred by the petitioning creditors and reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in a proceeding under this chapter—

(1) by a referee;

(2) by a special master;

(3) by the trustee and other officers, and the attorneys for any of them;

(4) by the attorney for the debtor; and

(5) by the attorney for the petitioning creditors.

Such compensation of referees and trustees shall not be governed by sections 40 and 48 of this Act.

SEC. 242. The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in connection with the administration of an estate in a proceeding under this chapter or in connection with a plan approved by the judge, whether or not accepted by creditors and stockholders or finally confirmed by the judge—

(1) by indenture trustees, depositaries, reorganization managers, and committees or representatives of creditors or stockholders;

(2) by any other parties in interest except the Securities and Exchange Commission; and

(3) by the attorneys or agents for any of the foregoing except the Securities and Exchange Commission.

SEC. 243 (11 U. S. C. 643). The judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred by creditors and stockholders, and the attorneys for any of them, in connection with the submission by them of suggestions for a plan or of proposals in the form of plans, or in connection with objections by them to the confirmation of a plan, or in connection with the administration of the estate. In fixing any such allowances, the judge shall give consideration only to the services which contributed to the plan confirmed or to the refusal of confirmation of a plan, or which were beneficial in the administration of the estate, and to the proper costs and expenses incidental thereto.

SEC. 244 (11 U. S. C. 644). Where a petition is filed under section 127 of this Act, the judge may allow, if not already allowed, reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in the pending bankruptcy proceeding—

(1) by a marshal, receiver, or trustee, as provided in subdivision g of section 48 of this Act, and the attorneys for any of them;

(2) by the attorney for the petitioning creditors;

(3) by the attorney for the bankrupt; and,

(4) by any other persons and the attorneys for any of them entitled under this Act to compensation or reimbursement in such bankruptcy proceeding.

SEC. 245 (11 U. S. C. 645). Where a petition is filed in a pending bankruptcy proceeding, the judge may allow reasonable compensation for services rendered and the proper costs and expenses incurred in such bankruptcy proceeding by a referee in bankruptcy. In fixing such compensation, the judge shall not be restricted by the provisions of section 40 of this Act.

SEC. 246 (11 U. S. C. 646). Upon the dismissal of a proceeding under this chapter, or the entry of an order adjudging the debtor a bankrupt, the judge may allow reasonable compensation for services rendered and reimbursement for proper costs and expenses incurred in such proceeding prior to such dismissal or order of adjudication by any persons entitled thereto, as provided in this chapter, and shall make provision for the payment thereof, and for the payment of all proper costs and expenses incurred by officers in such proceedings.

SEC. 247 (11 U. S. C. 647). The judge shall fix a time of hearing for the consideration of applications for allowances, of which hearing notice shall be given to the applicants, the trustee, the debtor, the creditors, stockholders, indenture trustees, the Securities and Exchange Commission, and such other persons as the judge may designate, except that, in the case of allowances for services and reimbursement in a superseded bankruptcy proceeding, notice need be given only to the applicants, the debtor, the trustee, and the unsecured creditors, and may be given to such other classes of creditors or other persons as the judge may designate. In the case of the dismissal of a proceeding under this chapter and the entry of an

order therein directing that bankruptcy be proceeded with, notice of the hearing to consider allowances need not be given to stockholders.

SEC. 248 (11 U. S. C. 648). In the case of the dismissal of a proceeding under this chapter and the entry of an order therein directing that a superseded bankruptcy be proceeded with, the compensation allowed by the judge, in the course of the proceeding under this chapter, to the referee, marshal, receiver, or trustee in the bankruptcy proceeding for services rendered by them in such bankruptcy proceeding shall be deemed to have been allowed in such bankruptcy proceeding, and such compensation shall be considered in connection with the making of future allowances therein or shall be readjusted, so as to comply with the provisions of this Act fixing their compensation in a bankruptcy proceeding.

SEC. 249 (11 U. S. C. 649). Any person seeking compensation for services rendered or reimbursement for costs and expenses incurred in a proceeding under this chapter shall file with the court a statement under oath showing the claims against, or stock of, the debtor, if any, in which a beneficial interest, direct or indirect, has been acquired or transferred by him or for his account, after the commencement of such proceeding. No compensation or reimbursement shall be allowed to any committee or attorney, or other person acting in the proceedings in a representative or fiduciary capacity, who at any time after assuming to act in such capacity has purchased or sold such claims or stock, or by whom or for whose account such claims or stock have, without the prior

consent or subsequent approval of the judge, been otherwise acquired or transferred.

SEC. 250 (11 U. S. C. 650). Appeals may be taken in matters of law or fact from orders making or refusing to make allowances of compensation or reimbursement, and may, in the manner and within the time provided for appeals by this Act, be taken to and allowed by the circuit court of appeals independently of other appeals in the proceeding, and shall be summarily heard upon the original papers.

SEC. 258 (11 U. S. C. 658). The judge shall make such provision as may be equitable for the protection of the obligations incurred by a receiver or trustee in such prior proceeding and for the payment of the reasonable costs and expenses incurred therein as may be allowed by the judge.

SEC. 276 (11 U. S. C. 676).

* * * * * *

c, the provisions of sections 77A and 77B of chapter VIII, as amended, of the Act entitled "An Act to establish a uniform system of bankruptcy throughout the United States," approved July 1, 1898, shall continue in full force and effect with respect to proceedings pending under those sections upon the effective date of this amendatory Act, except that—

(1) if the petition in such proceedings was approved within three months prior to the effective date of this amendatory Act, the provisions of this chapter shall apply in their entirety to such proceedings;

* * *.

ACT OF AUGUST 25, 1937, C. 777, 50 STAT. 810, 28 U. S. C. 572A

(a) it shall be unlawful for any party in interest, or any attorney for any party in interest, in any receivership, bankruptcy, or reorganization proceeding, in or under the supervision of any court of the United States, to enter into any agreement, written or oral, express or attorney of any other party in interest, in such proceeding for the purpose of fixing the amount of the fees or other compensation to be paid to any party in interest or any attorney of any party in interest in such proceeding, for services rendered in connection therewith when such fees or other compensation are to be paid from the assets of the estate in receivership, bankruptcy or reorganization. As used in this section, the term "party in interest" includes any debtor, creditor, receiver, or trustee and any representative of any of them.

GENERAL ORDERS IN BANKRUPTCY

GENERAL ORDER NO. 44.—APPOINTMENT OF ATTORNEYS

No attorney for a receiver, trustee or debtor in possession shall be appointed except upon the order of the court, which shall be granted only upon the verified petition of the receiver, trustee or debtor in possession, stating the name of the counsel whom he wishes to employ, the reasons for his selection, the professional services he is to render, the necessity for employing counsel at all, and to the best of the petitioner's knowledge all of the attorney's connections with the bankrupt or debtor, the creditors or any other party

in interest, and their respective attorneys. If satisfied that the attorney represents no interest adverse to the receiver, the trustee or the estate in the matters upon which he is to be engaged, and that his employment would be to the best interests of the estate the court may authorize his employment, and such employment shall be for specific purposes unless the court is satisfied that the case is one justifying a general retainer. If without disclosure any attorney acting for a receiver or trustee or debtor in possession shall have represented any interest adverse to the receiver, trustee, creditors or stockholders in any matter upon which he is employed for such receiver, trustee, or debtor in possession, the court may deny the allowance of any fee to such attorney, or the reimbursement of his expenses, or both, and may also deny any allowance to the receiver or trustee if it shall appear that he failed to make diligent inquiry into the connections of said attorney.

Nothing herein contained shall prevent the judge, in proceedings under section 77 of the Act, from authorizing the employment of attorneys who are attorneys of the corporation, or associated with its legal department, in connection with the operation of the business of the corporation by a trustee or trustees under subsection (c) of section 77, when such employment is found by the judge to be in the public interest in relation to such operation and is not adverse to the interests of the trustee or trustees or of the creditors of the corporation.

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SUPREME COURT OF THE UNITED STATES.

No. 183.—October Term, 1943.

B. H. Inness Brown, David Paine, Ethelbert Warfield, et al., Petitioners,

vs.

John Gerdes and James D. Carpenter, Jr., Trustees of Reynolds Investing Co., Inc., Debtor.

On Writ of Certiorari to the Court of Appeals of the State of New York.

[February 7, 1944.]

Mr. Justice Douglas delivered the opinion of the Court.

The question in this case is whether the New York court or the federal bankruptcy court has the power to fix the fees of petitioners who as attorneys represented the bankruptcy estate in litigation in the state courts. The New York Court of Appeals held that that jurisdiction rested exclusively in the bankruptcy court. 290 N. Y. 468. The case is here on a petition for writ of certiorari which we granted because of the importance of the problem under the Bankruptcy Act.

In January, 1939, a petition for reorganization of Reynolds Investing Co., Inc. was approved under Ch. X of the Bankruptcy Act. 52 Stat. 883, 11 U. S. C. § 501. In August, 1938, while the petition was pending but before its approval, the bankruptcy court authorized the debtor to commence an action in the New York courts to enforce and collect certain claims which the debtor had against its former officers and directors. See 28 N. Y. S. (2d) 622. It also authorized retention of petitioners as counsel in the suit. After the approval of the petition the respondent trustees were authorized to prosecute the action and to be substituted as plaintiffs. That was done; and other actions were instituted by the trustees under order of the bankruptcy court with petitioners as counsel. In 1941 before final judgments were obtained in any of the suits, the trustees discontinued petitioners' services. Thereafter petitioners, pursuant to a stipulation[1] which

[1] Respondents sought an order from the bankruptcy court directing petitioners to turn over their papers and memoranda. That motion was resisted by petitioners who claimed that the New York court had exclusive jurisdiction.

reserved respondents' right to question the jurisdiction of the state court, instituted this suit in that court to fix and enforce their liens on the actions under § 475 of the New York Judiciary Law.[2] Respondents' objection to the jurisdiction of the state court was overruled, the value of petitioners' services determined, and the liens fixed. Those orders were affirmed by the Appellate Division (264 App. Div. 852) but reversed by the Court of Appeals. And as we read the opinion of that court the basis of its decision was that "exclusive jurisdiction" to fix these fees was in the bankruptcy court (290 N. Y. 472, 473, 475), not that New York as a matter of local law or policy would not undertake to fix them because of the special circumstances of this case.

We agree with the Court of Appeals that the power to determine the amount of these fees rests exclusively in the bankruptcy court.

Sec. 77B, like § 77 of the Bankruptcy Act,[3] had as one of its purposes the establishment of more effective control over reorganization fees and expenses (*Dickinson Industrial Site, Inc.* v. *Cowan*, 309 U. S. 382, 388; *Callaghan* v. *Reconstruction Finance Corp.*, 297 U. S. 464, 469) in recognition of the effect which a depletion of the cash resources of the estate may have on both the fairness and feasibility of the plan of reorganization. *United States* v. *Chicago, Milwaukee, St. P. & P. R. Co.*, 282 U. S. 311, 333-340 (dissenting opinion). And Ch. X of the Chandler Act which took the place of § 77B set up even more comprehensive supervision over compensation and allowances (H. Rep. No. 1409, 75th Cong., 1st Sess., pp. 45-46) and provided a centralized control over all administration expenses, of which lawyers' fees are a part. *Watkins* v.

Thereupon a stipulation was entered into with the approval of the bankruptcy court whereby respondents withdrew their motion and petitioners agreed to institute a suit in the state court for fixation of their liens, if any. The parties reserved their right to question the jurisdiction of the state court or bankruptcy court over the matter.

[2] "From the commencement of an action, special or other proceeding in any court or before any state or federal department, except a department of labor, or the service of an answer containing a counterclaim, the attorney who appears for a party has a lien upon his client's cause of action, claim or counterclaim, which attaches to a verdict, report, determination, decision, judgment or final order in his client's favor, and the proceeds thereof in whatever hands they may come; and the lien cannot be affected by any settlement between the parties before or after judgment, final order or determination. The court upon the petition of the client or attorney may determine and enforce the lien."

[3] See Continental Bank v. Chicago, Rock Island & P. Ry. Co., 294 U. S. 648, 685; Reconstruction Finance Corp. v. Bankers Trust Co., 318 U. S. 163.

Sedberry, 261 U. S. 571. Sec. 241 gives the judge authority to fix "reasonable compensation for services rendered" by various persons, including attorneys for the trustees. Allowances may be made only after hearing and upon notice to specified persons and groups of persons. § 247. Where the reorganization supersedes a prior proceeding in either the federal or state court the bankruptcy court is the one which is authorized to allow the "reasonable costs and expenses incurred" in the prior proceeding. § 258. In all cases persons who seek compensation for services or reimbursement for expenses are held to fiduciary standards. § 249; *Woods* v. *City National Bank & Trust Co.*, 312 U. S. 262, 267-269. And § 250 contains special appeal provisions governing orders granting or denying allowances. *Dickinson Industrial Site, Inc.* v. *Cowan*, *supra*. Moreover, a plan of reorganization must provide "for the payment of all costs and expenses of administration and other allowances which may be approved or made by the judge." § 216(3). In addition the plan must provide, in furtherance of the purpose of the Act to protect the security holders against previous acts of mismanagement and to preserve all assets of the estate (S. Rep. No. 1916, 75th Cong., 3d Sess., p. 22; H. Rep. No. 1409, *supra*, pp. 42-44), for retention and enforcement by the trustee of all claims of the debtor or the estate not settled or adjusted in the plan. § 216(13). Finally, § 221(4) provides that in approving any plan the judge must be satisfied that "all payments made or promised" by the debtor, the new company, or any other person "for services and for costs and expenses" are not only fully disclosed but "are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge."

Thus Ch. X not only contains detailed machinery governing all claims for allowances from the estate. It also requires the plan to contain provisions for the payment of all allowances and places on the judge the duty to pass on their reasonableness. The approval of the plan of reorganization has been entrusted to the bankruptcy court exclusively. Even reports on plans submitted by the Securities and Exchange Commission are "advisory only". § 172. It could hardly be contended that the bankruptcy court might dispense with the finding required by § 221(2) that the plan is "fair and equitable, and feasible" and confirm the plan on another basis or delegate the task to another court or agency. *See Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, 114-

115; *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510. But if that cannot be done, it is difficult to see how a plan could be confirmed which left the approval of certain allowances to a state court. The finding as to allowances required by § 221(4) is as explicit and as mandatory as the finding of "fair and equitable, and feasible" required by § 221(2). On each Congress has asked for the informed judgment of the bankruptcy court, not another court or agency. In the present case the plan of reorganization which was approved in 1940 gave the trustees full power to retain or displace attorneys representing them; and it retained in the bankruptcy court continuing jurisdiction over all claims in favor of the debtor and the prosecution thereof. And in accordance with the express requirements of § 221(3) it left to the bankruptcy court the power to fix the "reasonable compensation" to be paid the attorneys of the trustees. Those requirements, prescribed by the Act, cause any conflicting procedure in the state courts to give way.[4] *Kalb* v. *Feuerstein*, 308 U. S. 433. The jurisdiction which Congress has conferred on the bankruptcy court is paramount and exclusive. *Gross* v. *Irving Trust Co.*, 289 U. S. 342. Thus the supervention of bankruptcy deprives a state court in which a receivership was pending, of power to fix the compensation of the receivers and their counsel who were appointed by the state court and who rendered service in the state proceedings. *Gross*, v. *Irving Trust Co.*, *supra*; *Emil* v. *Hanley*, 318 U. S. 515, 519.

Sherman v. *Buckley*, 119 F. 2d 280, which arose in ordinary bankruptcy, is relied upon for the contrary conclusion. In that case an action brought by the bankrupt had been pending in the state court for seven years before the adjudication in bankruptcy. The trustee obtained the consent of the bankruptcy court to allow the action to be prosecuted in the state court on behalf of the estate and to substitute attorneys other than those retained by the bankrupt. It was held that the state court could require as a condition upon the substitution the liquidation of the New York charging lien of the displaced attorneys. Whether that case was correctly decided on its facts we need not stop to inquire. It is sufficient to say that it does not state the correct rule of law under Ch. X of the Act.

[4] The submission of the matter to the state court with objections to its jurisdiction was a procedure which gave that "due regard for comity" suggested by the Court in Gross v. Irving Trust Co., 289 U. S. 342, 345.

It is said, however, that § 77B rather than Ch. X measures the jurisdiction of the bankruptcy court since the main suit was instituted in the state court prior to the effective date of Ch. X, September 22, 1938. See § 7. But the short answer is that the petition was approved after that date and the provisions of Ch. X were thus brought into play.[5] It is suggested that since § 23 of the Act[6] was applicable to reorganizations under § 77B but inapplicable[7] to those under Ch. X (§ 102), there was a greater limitation on the jurisdiction of the bankruptcy court over plenary suits at the time the main suit was instituted than there was after Ch. X became effective.[8] From that it is argued that since Congress left the enforcement of such claims to the state courts, it permitted them to control all incidents of the litigation including the fixing of attorneys' liens. Sec. 23 deals with questions of the jurisdiction of federal district courts, e. g., whether in suits by trustees in bankruptcy against adverse claimants the jurisdiction of the district courts rests on consent of the parties regardless of diversity of citizenship. *Schumacher* v. *Beeler*, 293 U. S. 367. The fact that the suits against the former officers and directors of the debtor could have been brought in the state courts alone does not advance the solution of the present problem. A bankruptcy trustee who by choice or by necessity resorts to a state court for the prosecution of a claim is of course bound by the adjudication made in the state proceeding. *Winchester* v. *Heiskell*, 119 U. S. 450; *Fischer* v. *Pauline Oil & Gas Co.*, 309 U. S. 294, 303. The state court has full control over the litigation. But even as an incident thereto, it may not take action which involves the performance of functions which Congress has entrusted to the bank-

[5] Even if the petition had been approved prior to the effective date of Ch. X its provisions would have applied in their entirety to the proceedings provided such approval was within three months prior to that date. § 276 (c) (1).

[6] Sec. 23 presently provides: "'a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants. 'b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67, and 70 of this Act.'"

[7] See Weinstein, The Bankruptcy Law of 1938 (1938), pp. 63-64; 2 Collier on Bankruptcy (14th ed.), pp. 435-436.

[8] See In re Standard Gas & Electric Co., 119 F. 2d 658.

ruptcy court. See *Eau Claire National Bank* v. *Jackson*, 204 U. S. 522, 537-538.

The suggestion has been made that New York could open its courts to the prosecution of such suits as the trustees instituted on condition that New York control the legal fees incident to the litigation; and that so long as New York did not discriminate against those asserting rights under the federal act such condition would be valid. Cf. *Douglas* v. *New York, N. H. & H. R. Co.*, 279 U. S. 377. It does not appear, however, that New York has followed that course. The fact that New York has adopted measures designed to protect attorneys practicing in its courts does not demonstrate that New York has made its control over the fees a condition to the use of its tribunals. There is no such indication in the opinion of the New York Court of Appeals. Thus we cannot say that New York has provided conditions for entry into its courts which collide with a Congressional enactment. We can only assume therefore that the case is no different in principle from the one where a state grants to creditors attachments in aid of the collection of their claims. There can be no doubt that such liens could be nullified by supervening bankruptcy whether the creditor be lawyer or merchant.

But if it is assumed that New York might have refused to entertain such suits as were brought against the old management (cf. *Monaco* v. *New York, N. H. & H. R. Co.*, 223 U. S. 1, 56-59) it does not follow that it could take jurisdiction of them but fail to apply any federal law in which those claims might be found. *Garrett* v. *Moore-McCormack Co.*, 317 U. S. 239. Where Congress has prescribed the rule to govern the compensation of those employed by the bankruptcy court, those claims are no less dependent on the federal rule because they are asserted as an incident to another suit. If the state court could disregard the federal rule in that situation, then any of the duties of administration which Congress has imposed on the bankruptcy court could be absorbed by the state tribunal. *Eau Claire National Bank* v. *Jackson*, *supra*. Congress has fixed the fees which various representatives or officers of the bankruptcy court may receive for their services. §§ 40, 48. Among these are the bankruptcy trustees. § 48 (c). As in the present case those trustees may at times choose to act as their own attorneys. But it would be novel doctrine indeed to hold that state courts could increase any maximum allowance which Congress might authorize bankruptcy trustees to receive from the

estate merely because the trustees rendered some of their services in state tribunals. Yet if Congress can protect bankruptcy estates by itself prescribing maximum fees for those representing or rendering service to the estate, it is not apparent why it may not reach the same result by delegating that authority to the bankrupcy court. Whatever doubts may have once existed as to the functions of a reorganization court, it is clear under this recent bankruptcy legislation that the approval of all fees as part of the plan has been entrusted to the bankruptcy court exclusively. The case is therefore controlled by the principle of *Hines* v. *Lowrey*, 305 U. S. 85. In that case we held that where an Act of Congress limited to ten dollars the fees for services in connection with veterans' War Risk Insurance claims, the New York court could not award a greater amount to an attorney representing a guardian of an insane veteran even where the guardian was appointed by the New York court. We reversed a judgment of the New York court granting the attorney $1500 for his services. The purpose of Congress to place the control of petitioners' fees in the bankruptcy court is no less clear than its purpose to limit the amount of fees in the *Hines* case. In each the federal rule is the supreme law of the land.

We only hold that the bankruptcy court has exclusive authority under Ch. X to fix the amount of allowances for fees. Whether the amount so fixed could be secured by a lien created by local law raises a question which we do not reach.

Affirmed.

Mr. Justice ROBERTS concurs in the result.

Mr. Justice FRANKFURTER, concurring.

1. Since 1789, rights derived from federal law could be enforced in state courts unless Congress confined their enforcement to the federal courts. This has been so precisely for the same reason that rights created by the British Parliament or by the Legislature of Vermont could be enforced in the New York courts. Neither Congress nor the British Parliament nor the Vermont Legislature has power to confer jurisdiction upon the New York courts. But the jurisdiction conferred upon them by the only authority that has power to create them and to confer jurisdiction upon them—namely the law-making power of the State of New York—enables

See, for instance, Minnesota v. Jones, 109 U.S. 513, 520.

them to enforce rights no matter what the legislative source of the right may be.

2. In short, subject to only one limitation, each State of the Union may establish its own judicature, distribute judicial power among the courts of its choice, define the conditions for the exercise of their jurisdiction and the modes of their proceeding, to the same extent as Congress is empowered to establish a system of inferior federal courts within the limits of federal judicial power, and the States are as free from control by Congress in establishing state systems for litigation as is Congress free from state control in establishing a federal system for litigation. The only limitation upon the freedom of a State to define the jurisdiction of its own courts is that implied by Article IV, Section 2 of the Constitution, whereby "The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States." The Constitution does not require New York to give jurisdiction to its courts against its will. But "If the State does provide a court to which its own citizens may resort in a certain class of cases, it may be that citizens of other States of the Union also would have a right to resort to it in cases of the same class". *Anglo-Am. Prov. Co. v. Davis Prov. Co. No. 1*, 191 U. S. 373, 474. The matter was well put by Judge Cuthbert Pound in connection with litigation under the Federal Employers' Liability Act in the state courts: "the State courts must make no hostile discrimination against litigants who come within the act in question; . . . they must treat litigants under the Federal act as other litigants are treated; . . . they are to act in conformity with their general principles of practice and procedure and are not to deny jurisdiction merely because the right of action arises under the act of Congress." *Murnan v. Wabash Railway Co.*, 246 N. Y. 244, 247.

3. The upshot of the matter is that "rights, whether legal or equitable, acquired under the laws of the United States, may be prosecuted in the United States courts, or in the State courts competent to decide rights of the like character and class; subject, however, to this qualification, that where a right arises under a law of the United States, Congress may, if it see fit, give to the Federal courts exclusive jurisdiction." *Claflin v. Houseman, Assignee*, 93 U. S. 130, 136-137. Whether a state court is "competent to decide rights of the like character and class", whether the particular litigation is to be tried by jury and, if so, how the

jury is to be composed, whether it is to be a jury of twelve or less, whether decision is to be by unanimity or majority, whether security is to be furnished and of what nature—in sum, whether a state court can take jurisdiction and what the incidents of the litigation should be—all these are matters wholly within the control of the State creating the court and without the power of Congress. See, for instance, *Minn. & St. Louis R. R.* v. *Bombolis*, 241 U. S. 211. As it was put by Mr. Justice Story in *Martin* v. *Hunter's Lessee*, 1 Wheat. 304, 330-331, "Congress cannot vest any portion of the judicial power of the United States, except in courts ordained and established by itself". Congress may avail itself of state courts for the enforcement of federal rights, but it must take the state courts as it finds them, subject to all the conditions for litigation in the state courts that the State has decreed for every other litigant who seeks access to its courts.

4. Congress from the beginning has allowed federally created rights to be enforced in state courts not only by the general implications of our legal system but also by explicit authorization. The nature of the obligation of the state court under such legislation has been most litigated in connection with the Federal Employers' Liability Act, and after thorough canvass the matter was thus summarized by Mr. Justice Holmes in *Douglas* v. *New Haven R. Co.*, 279 U. S. 377, 387-388. "As to the grant of jurisdiction in the Employers' Liability Act, that statute does not purport to require State Courts to entertain suits arising under it, but only to empower them to do so, so far as the authority of the United States is concerned. It may very well be that if the Supreme Court of New York were given no discretion, being otherwise competent, it would be subject to a duty. But there is nothing in the Act of Congress that purports to force a duty upon such Courts as against an otherwise valid excuse."

5. The simple fact is that from 1789 to this day no act of Congress has attempted to force upon state courts the duty of enforcing any right created by federal law on terms other than those on which like litigation involving rights other than federal rights is required to be conducted in a state court. It certainly has not done so by the Bankruptcy Act nor can any implication to that effect be derived from the Supremacy Clause of the Constitution. For the Supremacy Clause does not give greater supremacy to the Bankruptcy Act over the free scope of the States to determine what shall be litigated in their courts and under what

conditions, than it gives with reference to rights directly secured by the Constitution, such as those guaranteed by the Full Faith and Credit Clause, see *Anglo-Am. Prov. Co.* v. *Davis Prov. Co. No. 1, supra*, or with reference to the power exercised by Congress under the Commerce Clause, see *Minn. & St. Louis R. R.* v. *Bombolis, supra*.

6. The exercise of a right which Congress has not sought to exercise since 1789 and evidently has not exercised because of the constitutional relation of federal rights to their enforcement in state courts should not be read into Chapter X. c. 575, 52 Stat. 883, 11 U. S. C. § 501 *et seq.* We should hesitate long before we find that Congress has assumed the power to render unconstitutional state legislation by which access to a state court would be allowed to a litigant on no different terms than those which the State has prescribed for its own litigants to whom access to its courts is given in like cases. And certainly such a wholly novel doctrine of constitutional law should not be resorted to gratuitously when the case before us can be disposed of on the conclusive ground that the litigation conducted in the New York courts was conducted under an arrangement consonant with New York law, namely that the attorneys' fees were to be fixed not by the New York courts but by the Bankruptcy Court. See *Matter of Heinsheimer*, 214 N. Y. 361. Recognition that such is New York law and that therefore the remission of fee-fixing in this case to the Bankruptcy Court is not in conflict with that law appears from the opinion below: "as a matter of fact the retainer of these attorneys was subject to the condition that the amount of any fees would be fixed by the United States District Court." 290 N. Y. 468, 475. The disposition of this case requires neither the assumption made in the Court's opinion relating to New York law, nor the application given to Chapter X, both of which must be inescapable before we even reach the constitutional issue needlessly projected.

7. *Hines* v. *Lowrey*, 305 U. S. 85, does not touch this problem. That case involved § 500 of the World War Veterans' Act which limited to $10 the fee that may be allowed for services in pressing a claim before the United States Veterans' Bureau and made it a crime to charge more. A New York court granted a fee of $1500 for such services because the estate of the veteran was being administered by a committee appointed by the state court which had

appointed an attorney to press the claim before the Veterans' Bureau. Of course this Court held that a state court cannot sanction that which Congress has outlawed as a crime. The New York court in effect denied the authority of federal law to fix fees for litigation before a federal tribunal—a very different thing from denying to the State of New York the authority to fix fees for litigation in its own courts. The limitations in the *Hines* case fixed by Congress did not run counter to any requirement of New York law governing the conduct of suits in its courts. That case was not concerned with such a situation, and therefore could not possibly hold that, if New York had a policy for litigation in its courts contrary to that expressed by Congressional enactment, a federal right could be pursued in disregard of the conditions for entry into New York courts applicable to all other litigants. Congress has never said that it can subvert the declared policy of a State as to the manner in which, or the conditions under which, litigation in state courts should be conducted. The federal law in any field within which Congress is empowered to legislate is the supreme law of the land in the sense that it may supplant state legislation in that field, but not in the sense that it may supplant the existing rules of litigation in state courts. Congress has full power to provide its own courts for litigating federal rights. The state courts belong to the States. They are not subject to the control of Congress though of course state law may in words or by implication make the federal rule for conducting litigation the rule that should govern suits to enforce federal rights in the state courts. Surely it cannot be that should New York decide to regulate the public profession of the law by putting the determination of all attorneys' fees in charge of its courts, Congress could provide that actions thereafter brought in New York courts in the enforcement of federal rights shall not be subject to New York's fee system. I repeat, *Hines* v. *Lowery*, *supra*, gives no support whatever to a claim which was not involved in that case, which it did not consider, and which runs counter to the whole course of federal judiciary legislation and federal adjudication.

We ought not to go out of our way to embarrass consideration of such delicate questions in the working of our federal system whenever in the future they may call for decision by this Court.

Mr. Justice Jackson joins in this opinion.